A COMPANY'S ORGANS AND ITS OFFICERS AS ITS AGENTS IN COMPANY CONTRACTS

BY

SHANTHY a/p THURAISINGHAM

A dissertation submitted in partial fulfillment of the requirements for the Degree of Master of Laws by Coursework and Dissertation.

Faculty of Law
University of Malaya
Kuala Lumpur

March 1998

Synopsis

This dissertation proposes to examine the organs of the Company and its officers as its agents in company contracts. It will also examine the law in England and Australia pertaining to the said subject and recommend whether Malaysia should be prompted to adopt the statutory reforms of these countries.

It is generally said that the human agency through which the capacity of the company can operate or manage and conduct itself lies either in the shareholders acting together in general meeting or the board of directors, the two principal organs of the company. Both these organs have an organic quality of their own and in theory they can exercise all the powers of the company under its memorandum or articles and those conferred to it by statute. However, there is a legal as well as a commercial necessity to divide the powers of the company between these two organs.

This dissertation will firstly look into the various powers of this organs, the source of their powers and the autonomous characteristics of these organs in Malaysia , England and Australia.

The dissertation will then go on to discuss the issue that in practice, outsiders rarely deal with the board of directors or the members in general meeting. More often, their relationship with the company involves dealing with the agents or employees of the company. Companies are capable of being bound by the acts of its agents in the same way as natural persons: s.35(4) of the Companies Act 1965(hereinafter referred to as 'the Act'). This involves the application of the principles of agency law, in particular the question whether those who purport to act

on the company's behalf have the authority to do so. Agency law has several distinct features in its application to companies and in particular is the doctrine of ultra vires.

The study will critically examine the legal capacity and competence of the company as limited by the law. The Act requires a company to state in the memorandum of association the objects of the company. Section 18(1) of the Act sets out the minimum content requirement of the memorandum of association. Amongst others, the memorandum of association was required to contain an objects clause that specifies the range of activities the company was permitted to engage in. The objects clause was regarded as important from the point of view of the company's shareholders and creditors. They were entitled to expect that the money they invested or lent to the company would be applied in carrying the business listed in the objects clause. The importance of the objects clause was reinforced by the common law doctrine of *ultra vires.* The doctrine provided that any contract made by the company that was not in furtherance of a transaction specified in the objects clause was void. The dissertation will then go on to discuss the fact that role of the *ultra vires* doctrine as explained by the judges, was to prevent insidious enlargement of a company's capacity as a result of indiscriminate exercises of powers for purposes that are neither ancillary or reasonably incidental to the pursuit of authorised objects by rejecting such exercise of powers as being null and void. Although this may result in a very harsh treatment of an outsider who is a *bona fide* purchaser dealing with the company in good faith without notice, this remains necessary if the whole rationale of the *ultra vires* doctrine is to be preserved. Further the dissertation will analyse the common law and statutory development of this doctrine and a comparison will be made with the English and Australian position.

This dissertation will also examine the point that a company may enter into a contract indirectly through an agent. The agent may be an officer or employee of the company. Whether a company will be liable under a contract for the acts of an officer or agent is governed under the general law of agency. These agency principles have been modified by the common law and the Act so as to recognise the abstract nature of companies.

This dissertation will then discuss the fact that whenever there is a delegation of power to an agent, that agent is given some sort of authority by the principal. This authority is the actual authority of the agent. This authority may be express or implied authority. Express authority is that which is expressly conferred upon the agent. Implied authority is not expressly stated; it is authority implied by the circumstances. This may be of two forms: authority to do things incidental to matters that the agent is expressly authorised to do so, and authority to do things that a person in that position usually does. This type of implied authority is sometimes known as "customary" or "usual" authority. This dissertation will look into the various authorities given to the agents.

Further, the dissertation will discuss the fact that sometimes the authority of an agent to do certain acts depends on compliance with certain formalities or there is some irregularity in the management which vitiates the authority conferred upon the agent which a party outside the company has no way of determining whether the company's internal regulations have been complied with. However, the law does not require an outside party to do so. If an agent has an apparent authority to do an act, a person dealing with the company is entitled to assume that all matters of internal management and procedures prescribed by the articles of association have been complied with. This is known as the "rule in *Turquand's* case" or the "indoor management rule".

The dissertation will examine the rule in *Turquand's* case and its' exceptions as it is applied in Malaysia and the common law as it has been codified in England .

However, the Rule has been criticised because of uncertainty which has arisen from a large body of case law.

As a consequence, in Australia, the common law principles discussed above have been now been replaced by statutory provisions. The principles are now contained in ss. 164 to 166 of the Corporations Law 1990(herein after referred to as the 'Corporation Law'). These provisions are based around six protective assumptions set out in s.164(3) of the Corporation Law and are subject to the limitations in s.164 (4). The Australian provisions are an attempt to make a comprehensive reform of the unsatisfactory judge-made law on the subject of this dissertation. The dissertation will critically examine these statutory provisions in detail and also consider the extent to which the statutory provisions in Australia could be adopted in Malaysia.

In conclusion, it is stated that in Malaysia the Rule in *Turquand's* case reigns supreme together with its obscurities and inadequacies. Whether the Malaysian legislatures may be prompted or be tempted to venture into a statutory reform like in Australia or as in England remains to be seen. For the time being in Malaysia the subject of this dissertation continues to be regulated by common law, which to an Australian or English observer, may look a little out of date. Finally, it is stated that while reform is welcome and necessary, a bland automatic adoption of foreign legislation may not be to Malaysia's advantage. Care must be taken to ensure that we do not import foreign legislation with all their deficiencies.

It is hoped that this dissertation serves to clarify the position of the organs and officers of a company and their relationship with the outsider to an appreciable extent.

Discussion and study relating to the relevant law and cases cover the period up to December 1997.

Acknowledgement

This dissertation is in partial fulfilment for the Masters of Law degree conferred by the University of Malaya. In researching this work, I have received expert advice and assistance, been the beneficiary of academic excellence, tremendously uplifted morally and spiritually and on the whole, been motivated in more ways than can be enumerated. For all this, I am deeply and humbly indebted to the following persons without whose patience , guidance and motivation this work would not have been possible.

My sincere and warmest thanks to :

- my supervisor, Professor Balan, for his tremendous, pleasantly exercised patience, tireless encouragement, valuable advice and comments and the wholly unselfish sharing of his vast expert academic excellence and knowledge throughout the course of this study; for always being available and never too busy to entertain a query or to clarify a point even during his hectic schedule or during his leave;
- my husband, Dr.S.P.Rachagan for having taken time off from his hectic schedule to proof read this dissertation;
- my colleagues and friends for their encouragement;
- my family members for their patience and understanding.

Table of Contents

Table of Cases

Hambro v. Burnand [1904] 2 KB 10

Hawkesbury Development Co. Ltd. v. Landmark Finance Pty.Ltd. (1970) 92 WN (NSW)

Hely – Hutchinson v. Brayhead Ltd.[1968] 1 QB549

Heng Wan v. Selangor Rice Mill Co. [1967] 2 MLJ 44

Hickmen v. Kent & Romney Marsh Sheepbreeders' Association [1919] 1 Ch. 881

Hogg v. Crompton Ltd. [1967] Ch. 254

Howard Smith Ltd. v. Ampol Petroleum Ltd. & Ors. [1974] AC 821

Howard v. Patent Ivory Manufacturing Co. (1888) 38 ChD 156

Hughes v. NM Superannuayion Pty. Ltd. (1993) 11 ACLC 923

Imperial Hydropathic Hotel Co., Blackpool v. Hampson (1882) 23 Ch. D. 1

Irvine v. Union Bank of Australia (1877) 2 App Cas 366

John Shaw & Sons (Salford) Ltd v. Peter Shaw [1935} 2 KB 113

Kelapa Sawit (Teluk Anson) Sdn. Bhd. v. Dr. Yeoh Kim Leng & Ors. (1991) !1 ML 301

Kreditbank Cassel v. Schenkers [1927] 1KB 826

Lloyds Bank Ltd. v. The Chartered Bank of India, Australia and China [1929] 1 KB 40

Lyford v. Media Portfolio Ltd. (1989) 7 ACLC 271

Mahoney v. East Holyford Mining Co. (1875) LR 7 HL 869

Marshall's Valve Gear Co. Ltd. v. Manning Wardle & Co. Ltd. [1906] 1 CH. 267

Mohamed bin Othman & Anor. V. Abdul Shattar bin Abdul Rahman & Ors. [1987} 2 MLJ 695

Morris v. Kanssen [1946} AC 459

National Road and Motorists' Association v. Parker (1986) 4 ACLC 609

Newlands v. National Employers' Accident Association (1885) 54 LJ

Richard Brady Franks Ltd. v. Price (1937) 58 CLR 112

Rolled Steel Products (Holdings) v. British Steel Corporation (1984) B.C.L.C. 466

Royal British Bank v. Turquand (1856) 119 ER 886

Ruben v. Great Fingall Consolidated [1906] AC 439

Salomon v. A Salomon and Co. Ltd. [1897} AC 22 House of Lords

Scott v. Scott [1943] 2 KB 113

Southern Foundries (1926) Ltd. v. Shirlaw [1940] 2 All ER 445 (House of Lords)

Storey v. Advance Bank of Australia Ltd. (1993) 11 ACLC 629

Underwood Ltd. v. Bank of Liverpool [1924] 1 KB 715

Vrisakis v. ASC (1953) 11 ACLC 763

Wong Kim Fatt v. Leong & Co. Sdn. Bhd. & Anor [1976] 1 MLJ 140

Woodland Development Sdn. Bhd. v. Chartered Bank [1986] 1 MLJ 84

Worchester Corsetry Ltd. v. Whitting [1936] 1 Ch. 640

Table of Statutes

LIST OF ABBREVIATIONS

The following abbreviations of law reports are used:-

AC App. Cas	Law Reports, Appeal Cases.
All ER	All England Law Reports.
ALJR	Australian Law Journal Reports.
BCLC	Butterworths Company Law Cases Butterworths (London)
CLR	Commonwealth Law Reports (Aust.).
DLR	Dominion Law Reports (Canada)
JMLC	Journal of Malaysian & Comparative Law
KB	Law Reports, Kings Bench.
LJ	Law Journal
LJ Ch.	Law Journal Reports, Chancery
LR Ch. App.	Law Reports, Chancery Appeal Cases.
LR QB	Law Reports , Queens Bench.
MLJ	Malayan Law Journal.
MLR	Malayan Law Review
NSWLR	New South Wales Law Reports.
NZLR	New Zealand Law Reports.
QB	Law Reports , Queens Bench.
QJPR	Queensland Justice of Peace Reports (Aust.).
SR	New South Wales State Reports.
VLR	Victorian Law Reports (Australia).

INTRODUCTION

The separate legal personality of a company was firmly established at common law in the case of *Salomon v A Salomon and Co. Ltd*[1] . A direct consequence of the incorporation of a company is that the company has a legal personality of its own which is distinct from its corporators. This means that the company has its own legal capacity to enjoy rights, assume obligations and incur liabilities and perform duties independently of the corporators. However, as a corporation is an artificial person, its capacity can only operate through some human agency; it has no mind of its own any more than it has a body of its own.

The human agency through which the capacity of the company can operate or manage and conduct itself lies either in the shareholders acting together in general meeting or the board of directors, the two principal organs of the company. Both these organs have an organic quality of their own and in theory they can exercise all the powers of the company under its memorandum or articles and those conferred to it by statute. However, there is a legal as well as a commercial necessity to divide the powers of the company between these two organs. The first chapter of this thesis will look into the various powers of this organs, the source of their powers and the autonomous characteristics of these organs in Malaysia , England and Australia.

In practice, outsiders rarely deal with the board of directors or the members in a general meeting. More often, its relationship with the company involves dealing with its agents or employees. Companies are capable of being bound by the acts of its agents in the same

[1] [1897] AC 22 House Of Lords

way as natural persons: s.35(4) of the Companies Act 1965(hereinafter referred to as 'the Act'). This involves the application of the principles of agency law, in particular the question whether those who purport to act on the company's behalf have the authority to do so. Agency law has several distinct features in its application to companies and in particular is the doctrine of ultra vires.

However, it must be stated that an individual has the natural legal power to enter into any binding contractual relationship. In contrast, companies have to be endowed with these capabilities and powers by the law. It follows that unlike an individual, a company may only legitimately exercise powers that have been endowed by law.

A company's legal capacity and competence is thus limited because the Act requires a company to state in the memorandum of association the objects of the company. Section 18(1) of the Act sets out the minimum content requirement of the memorandum of association. Amongst others, the memorandum of association was required to contain an objects clause that specifies the range of activities the company was permitted to engage in. The objects clause was regarded as important from the point of view of the company's shareholders and creditors. They were entitled to expect that the money they invested or lent to the company would be applied in carrying the business listed in the objects clause. The importance of the objects clause was reinforced by the common law doctrine of *ultra vires*. The doctrine provided that any contract made by the company that was not in furtherance of a transaction specified in the objects clause was void.

The role of the *ultra vires* doctrine as explained by the judges was to prevent insidious enlargement of a company's capacity as a result of indiscriminate exercise of powers for purposes that are neither ancillary or reasonably incidental to the pursuit of authorised

objects by rejecting such exercise of powers as being null and void. Although this may result in very harsh treatment to an outsider who is a *bona fide* purchaser dealing with the company in good faith without notice, this remains necessary if the whole rationale of the *ultra vires* doctrine is to be preserved. The common law and statutory development of this doctrine will be explored in Chapter 2 of this thesis and a comparison will be made with the English and Australian position.

As stated earlier, a company is an abstract entity, and it can only enter into contracts through the actions of a natural person. Section 35 (4) of the Act provides that so far as the of making a contract is concerned, a person acting under the express or implied authority of a company, may make a contract in the name of or on behalf of the company in the same manner as if that contract were made by a natural person. This indicates that a company may enter into a contract directly through one of its organs, usually the board of directors, or through a person who represents the mind and will of the company. This type of situation is governed under the organic theory of company law which largely lies outside the law of agency but draws upon it.

A company may also enter into a contract indirectly through an agent. The agent may be an officer or employee of the company. Whether a company will be liable under a contract for the acts of an officer or agent is governed under the general law of agency. These agency principles have been modified by the common law and the Act so as to recognise the abstract nature of companies. The agency rules which are applicable to

companies are subject to the common law rules and to the doctrine of constructive notice and a special set of principles known as the "rule in *Turquand's case*"[2] and its exceptions.

Whenever there is a delegation of power to an agent, that agent is given some sort of authority by the principal. This authority is the actual authority of the agent. This authority may be express or implied authority. Express authority is that which is expressly conferred upon the agent. Implied authority is not expressly stated; it is authority implied by the circumstances. This may be of two forms: authority to do things incidental to matters that the agent is expressly authorised to do so,[3] and authority to do things that a person in that position usually does.[4] This type of implied authority is sometimes known as "customary" or "usual" authority. Chapter 3 will look into the various authorities given to the agents.

Sometimes the authority of an agent to do certain acts depends on compliance with certain formalities or there is some irregularity in the management which vitiates the authority conferred upon the agent. A party outside the company has no way of determining whether the company's internal regulations have been complied with. However, the law does not require an outside party to do so. If an agent has an apparent authority to do an act, a person dealing with the company is entitled to assume that all matters of internal management and procedures prescribed by the articles of association have been complied with. This is known as the "rule in *Turquand's* case" or the "indoor management rule".

---

[2] *Royal British Bank v. Turquand (1856) 119 ER 886.*

[3] *Pole v. Leask* (1860) 28 Beav 562, 575 per Sir John Romilly MR (Master of the Rolls' Court, England); affirmed by the House of Lords. (1863) 33 LJ Ch 155

[4] *Hely - Hutchinson v. Brayhead Ltd.* [1968] 1 QB 549, 583 per Lord Denning MR (Court of Appeal, England).

Hence, person's dealing with a company and contracting in good faith may assume that

> "acts within its constitution and powers have been properly and duly performed and are not bound to inquire whether acts of internal management have been regular." [5]

The application of this rule gives rise to a presumption which prevents the company from avoiding a contract by relying on the fact that the proceedings were irregular and the person acting for the company was unauthorised to do so. This serves to protect persons "who are entitled to presume, just because they cannot know, that the person with whom they deal has the authority which he claims"[6] .

At common law, the doctrine of constructive notice operated against outsiders dealing with companies. However, this doctrine did not operate where the directors or other agents of a company acted outside their authority but this was not apparent from the articles or other public documents of the company. The rule specifically states that while persons dealing with a company are taken to have constructive notice of the contents of the company's public documents, they need not go further to ensure that the internal proceedings of the company have been properly carried out. In fact, the outsider can assume that these proceedings were properly carried out.

The rule in *Turquand's* case and its' exceptions as it is applied in Malaysia and the common law as it has been codified in England will be discussed in Chapter 4..

---

[5] Halsbury's Laws of England 4th ed 1988 Vol 7 (1) par 980. This statement was approved by Lord Simonds in *Morris v Kanssen* [1946] AC 459 at p 474.

[6] per Lord Simonds in *Morris v Kanssen* (above)

However, the Rule has been criticised because of uncertainty which has arisen from a large body of case law. Professor Gower observed:

> " *Unhappily its obscurity increases in direct proportion* to the literature upon it, and only its undoubted practical importance makes it essential to devote some space to it even at the risk of further obfuscation."

Gower commented that the history of the development of the Rule saw an increase in the limitations to which the rule was subject. These limitations have become so extensive that the object of the rule has been obscured.

> " The result is that the law has become a jungle of irreconcilable decisions to the benefit of no one save the legal profession. If this branch of the law is ever codified the draftsman will be well advised to ignore all case law of the present century and to go back to the first principles and the judgments of the founding fathers of our modern company law. Unhappily a textbook writer has to state the law as he finds it and not as it ought to be."[7]

As a consequence, in Australia, the common law principles discussed above have been now been replaced by statutory provisions. The principles are now contained in ss. 164 to 166 of the Corporations Law 1990(hereinafter referred to as the 'Corporation Law'). These provisions are based around six protective assumptions set out in s.164(3) of the Corporation Law and are subject to the limitations in s.164 (4). The Australian provisions are an attempt to make a comprehensive reform of the unsatisfactory judge-made law on the subject of this dissertation. Chapter 5 will discuss these statutory provisions in detail

[7] Thompson "Company Law" Doctrines and Authority to Contract (1956) Univ of Toronto LJ 248 at p 254

and also consider the extent to which the statutory provisions in Australia could be adopted in Malaysia.

CHAPTER 1

THE ORGANS OF THE COMPANY

1.1 Introduction

Section 16 (5) of the Companies Act 1965[1] (hereinafter referred to as 'the Act') provides as follows :

> "On and from the date of incorporation ... the subscribers to the memorandum together with such other persons as may from time to time become members of the company shall be a body corporate by the name contained in the memorandum capable forthwith of exercising all the functions of an incorporated company and of suing and being sued and having perpetual succession ... with power to hold land but with such liability on the part of the members to contribute to the assets of the company in the event of it being wound up as is provided by this Act."

This section identifies a company as a separate legal personality. The separate legal personality of a company was firmly established at common law in the case of *Salomon v A Salomon and Co. Ltd*[2] . A direct consequence of the incorporation of a company is that the company has a legal personality of its own which is distinct from its corporators. This means that the company has its own legal capacity to enjoy rights, assume obligations and incur liabilities and perform duties independently of the corporators. However, as a corporation is

---

[1] Act No. 125

[2] [1897] AC 22 House Of Lords

an artificial person, its capacity can only operate through some human agency; it has no mind of its own any more than it has a body of its own. In the case of *Northern Counties Securities Ltd. v. Jackson and Steeple Ltd*[3] . Walton J. said:

> "... the company as such was only a juristic figment of the imagination, lacking both a body to be kicked and a soul to be damned. From this it followed that there must be some one or more persons who did, as a matter of fact, act on behalf of the company, and whose acts therefore must, for all practical purposes, be the acts of the company itself."[4]

The human agency through which the capacity of the company can operate or manage and conduct itself lies either in the shareholders acting together in general meeting or the board of directors, the two principal organs of the company. Both these organs have an organic quality of their own and in theory they can exercise all the powers of the company under its memorandum or articles and those conferred to it by statute. However, there is a legal as well as a commercial necessity to divide the powers of the company between these two organs.

1.2 The Board of Directors

The board of directors is usually charged with the function of managing the company's business.[5] Typically the board is given the powers of the company other than those that the Act or the memorandum and articles of association

---

[3] [1974] 2 All ER 625

[4] Ibid, at p. 634.

[5] Table A arts.73 –78 provide an example of the common form of articles.

reserve for the members. In managing the company's business the board may make both strategic as well as operational decisions. However, in many cases the actual day to day management of a company is delegated to a managing director or managers or the company secretary. The larger the company, the more likely the board will concern itself only with broad policy, leaving operational decisions to delegates. The board's function in relation to such persons is to supervise them to ensure that they keep within the sphere of activity allotted to them.

The Act also envisages that the board will ensure that the company is run in accordance with the law. This is sometimes done by ensuring that the board is responsible for compliance with various sections. Therefore the board is responsible for the appointment of the company secretary and the company's first auditors.[6]

Also, the board must also ensure that proper accounting records are kept and that the accounts are laid before the members at the annual general meeting and that the provisions of the Act concerning the accounts are observed.[7]

Thus, it may be said that the board of directors has a threefold function. First, it makes decisions on behalf of the company within the sphere that has been delineated to it. Secondly, the board is responsible in general for supervising the company's agents and employees in the discharge of their duties. Thirdly, the

[6] s. 139(1) and s.172(1) of the Act respectively.

[7] s.171 of the Act

directors are generally responsible for ensuring that the company is run in accordance with the Act.[8]

However, the function of any particular director depends upon the arrangement between him and the company and the company's organizational set-up.

1.2.1 Directors

Under section 4(1) of the Act, the term company officer generally includes a director. A director is someone appointed to carry out the day-to-day running and control of the company. A director may be appointed by the members at the annual general meeting or the articles may provide that a certain person or body will have the power to appoint the directors of the company (as illustrated in the case *Raffles Hotel v. Malayan Banking (No.2)*[9])

It is obvious from the Act that the test which determines whether a person is a director is one of function and not of name. Therefore, anybody who functions as a director will be vested with the duties and liabilities of a director even though he may not be officially appointed to the office of director. The concept of someone not on the board but controlling the company has reached the point where the existence of a "shadow director" has been acknowledged by section 4 of the Act. A shadow director is a person in accordance with whose directions the directors are accustomed to the act. However, a person is not a shadow director merely because the directors of the company receive advice from him

---

[8] "Company Law" - Walter Woon (Law & Tax, Asia Pacific) (1997)

[9] [1966] 1 MLJ 206 (Court of Appeal, Singapore).

which is part of his professional service. Hence, a lawyer who advises directors in his professional capacity will not be deemed a director of the company.

Section 122 (1) of the Act states that every company must have at least two directors at any one time. Further section 122 (2) states that directors have to be natural persons and section 122 (3) states that the first directors must be named in the memorandum or articles of association.

In the case of public companies or their subsidiaries, section 127 of the Act states that the directors must not be above the age of 70 years of age. Also, a director of a public company is bound to inform the company in writing of the date he will turn 70 years old and he must do so within 14 days after he becomes a director. However, a person above the age of 70 years may be appointed or re-appointed as a director if a resolution supported by 75% of the members is passed approving the appointment. The appointment will only be until the next general meeting.

Section 129 (1) of the Act provides that the act of the director is valid notwithstanding any defect which may later be discovered in his appointment or qualification. However what the provisions cannot do is to cure a situation where there has been a total absence of appointment as opposed to a mere slip or irregularity in appointment as illustrated in the case of *Morris v. Kanssen*[10] .

The law pertaining to the removal of directors in a public company is different from that applicable to a private company.

---

[10] [1946] AC 459

In the case of a public company, it is not possible to have irremovable directors. Section 128(1) of the Act provides that a public company may always remove a director by ordinary resolution, notwithstanding anything contained in the company's memorandum or articles of association or in any agreement that may exists with the director. Section 128(2) of the Act states that a special notice must be given of such a resolution notwithstanding anything to the contrary stated in the memorandum or articles of association or in any agreement that may exists with the director. Special notice means that the directors proposing the resolution must give the company notice of their intention to move the resolution at least 28 days before the meeting and the director who is to be removed is entitled to make representation in writing to the company, which is bound to circulate it. At the meeting the director has a right to have his defence heard. Section 128(7) of the Act states that s.128 coexists with any other powers to remove directors which might exists apart from the section. Therefore, if the articles of association allow the removal of the directors, he may be removed in accordance with the articles of association. However, the procedure set out in s.128(2) of the Act must be adhered to.

The power to remove a director of a private company would usually be governed by the company's articles of association. A company's articles may usually provide that it may by ordinary resolution remove a director before the expiration of his period of service. Table A article 69 is an example of such an article. In the absence of such an article, a director whose term of office is specified in the articles may not be removed before the expiration of that term

until the articles have been altered appropriately as illustrated in the case of *Imperial Hydropathic Hotel Co., Blackpool v. Hampson* [11] .

If a director has a separate contract of service with the company, the removal of the director in question before his term expires will be in breach of contract for which damages may be obtained. This can be enunciated from the case of *Southern Foundries (1926) Ltd. v. Shirlaw*[12] . A director removed under section 128(1) of the Act also retains his rights to obtain compensation in accordance with any contract that he might have with the company. This is provided by section 128(7) of the Act.

1.3. Members in General Meeting

It was stated in the case of *Raja Khairulzaman Shah v. Zaman Indah Sdn. Bhd.*[13] the fact that a person owns shares does not by itself. make him a member of the company. There are only three ways of becoming a member of a company. First, section 16(6) of the Act states that the subscribers to a memorandum are automatically members of the company; they become members *ipso facto* on the incorporation of the company. Secondly, by s.123 (2) of the Act where a person has signed and lodged an undertaking to take and pay for his qualification shares, he shall, as regards those shares, be in the same

---

[11] (1882) 23 Ch. D. 1

[12] [1940] 2 All ER 445 (House Of Lords)

[13] [1979] 2MLJ 181.183 per Abdoolcader J.

position as if he had signed the memorandum for that number of shares. Third, s.16 (6) goes on to state that any person who agrees to become a member and whose name is on the register of members is a member of the company.

The term "shareholder" is often loosely used synonym for "member". However, a member need not be a shareholder. The obvious case is when the company does not have a share capital. Nor is a person who owns shares in a company necessarily a member; as it is possible to purchase shares on the Stock Exchange without being registered as the holder of the shares in the company's register of members. Therefore, a person may be a shareholder in the sense of owning shares in the company without being a member. A holder of shares who is not a member is not entitled to exercise any of the rights of membership, nor is he subject to the liabilities of a member.

1.3.1 Members' Rights

All members' of companies have certain rights conferred on them by the Act, the articles or the general law. Members are entitled to the following rights:-

a) to have the memorandum and the articles observed - s.33(1) of the Act;

b) to restrain ultra vires acts - s.20(a) of the Act;

c) to have access to company's records and to have certain information provided to them - s. 160(2), s.141(5), s.115(3) of the Act;

d) to attend and vote at general meetings – s.148(1) of the Act;

e) to be treated fairly – s.181 0f the Act.

These rights are personal rights of the member, and the company or any other person cannot generally interfere with the exercise of such rights.

1. 4 Division of Corporate Powers Between Board and General Meeting

Shareholders cannot operate, manage or conduct all functions of a company. This is because the diversity of individual interests amongst shareholders would not promote efficient and orderly management of the affairs of a company. Furthermore, there is the inconvenience in having to assemble shareholders together to debate upon every decision or to conduct business on a daily basis. The exception is when the company has very few shareholders.

From the legislative point of view, the necessity to control the affairs of the company also requires that there should be a definite individuals upon whom the law can impose responsibility or enforce compliance with the statutory provisions. As a consequence, it is a statutory requirement under s.122(1) of the Act that a company must have at least two directors. For these reasons, commercial and legal expediency dictate that the powers of management should be divided between the board of directors and the shareholders in the general meeting and that ideally the major portion of management powers should vest in a small group of people, namely, the board of directors.

1.4.1 Consequence of Division of Powers

Once powers are divided between the board and the shareholders in a general meeting, whether under the articles of association or the Act, the general resulting consequence is that one organ is autonomous of the other and no organ may usurp or interfere with the exercise of powers by the other.[14]

However, the general meeting may nonetheless be considered the supreme organ in the sense that if there is a breakdown in the machinery of the board of directors in relation to the exercise of powers exclusively vested in them, the general meeting may intervene by assuming the powers but only for purposes of resolving the impasse. There are however English cases dealing with the power to issue shares which does not nicely fit into the principle of autonomy. In *Hogg v. Cromphorn Ltd.*[15] and *Bamford v. Bamford*[16] where directors exercised their power to issue share for an improper purpose, a general meeting had a power to intervene by ratifying the improper exercise of power.

1.5 Sources of Management Powers

There are three sources from which management powers are derived. The first source is common law, the second is the articles of association which is

[14] *National Roads and Motorists' Association v. Parker* (1986) 4 ACLC 609

[15] [1967] Ch.254.

[16] [1970] Ch. 212.

regarded as a kind of statutory contract between the company and each of its members and the third source is the Act itself.

1.5.1. Articles of Association

The articles of association of a company are provisions which regulate the internal management and operation of the company. Section 33(1) of the Act gives contractual effect to the articles. It provides that they have the effect of a contract under seal between the company and each member[17] and members inter se[18] under which each of them agrees to observe and perform the provisions of the articles of association as in force for the time being so far as the provisions are applicable to them. This is illustrated in the case of *Wong Kim Fatt v. Leong & Co. Sdn. Bhd.& Anor.*[19]

It also invariably establishes a hierarchy of powers which is divided between the board of directors and shareholders in general meeting. Where powers are divided, effect will be given to the division.

It would not be quite feasible to set out specifically the respective powers of each of the two organs individually. Hence, there is always a provision vesting all general powers of management in the board of directors in addition to provisions delegating specific powers. Most companies adopt Article 73 of Table A articles of association as the provision vesting general powers of

---

[17] *Hickmen v. Kent & Romney Marsh Sheep – Breeders' Association [1919] 1 Ch 881*

[18] *Rayfield v. Hands [1960] Ch 1*

[19] [1976] 1 MLJ 140

management in the board of directors.

1.5.2 General Powers of Management vested in the Board: art.73 of TableA

Article 73 of Table A provides as follows:-

The business of the company shall be managed by the directors who may pay all expenses incurred in promoting and registering the company, and may exercise all such powers of the company as are not, by the Act or by these regulations, required to be exercised by the company in general meeting, subject to the provisions of the Act, and to such regulations, being not inconsistent with the aforesaid regulations or provisions, as may be prescribed by the company in general meeting; but no regulation made by the company in general meeting shall invalidate any prior act of the directors which would have been valid if that regulation had not been made.

The case of *Automatic Self-Cleansing Filter Syndicate Co. Ltd. v. Cuninghame*[20] makes it clear that who has what powers under the articles of association depends upon the construction of the articles of association. Where specific powers are laid down, there will not be much difficulty in deciding the issue. However, the interpretation to be given to art.73 of Table A which vests general powers of management and control in the board of directors has given rise to considerable difference of opinion.

---

[20] [1906] 2 Ch. 34.

Cozens-Hardy LJ in the above case held :

> "It has been decided that the articles of association are a contract between the members of the company inter se. That was settled finally by the case of *Browne v. La Trinidad* (1887) 37 Ch D 1, if it was not settled before. We must therefore consider what is the relevant contract which these shareholders have entered into, and that contract, of course is to be found in the memorandum and articles. ..., but it seems to me that the shareholders have by their express contract mutually stipulated that their common affairs should be managed by certain directors to be appointed by the shareholders in the manner described by other articles, and such directors be will liable to be removed only by special resolution. If you once get a stipulation of that kind in a contract made between the parties, what right is there to interfere with the contract, apart, of course, from any misconduct on the part of the directors? There is no such misconduct in the present case"[21] .

1.5.2.1 Construction of Article 73 of Table A

Where it is intended that certain inherent powers of shareholders are to be excluded and emplaced in the hands of the management, clear words must be used to displace those inherent powers. One of the inherent powers of

[21] Ibid, at p 44

shareholders is the right to appoint directors in general meeting as illustrated in the case of *Worcester Corsetry, Ltd. v. Witting*[22].

The general power of management and control vested in the board in terms of art.73 of Table A is clearly made subject to the provisions of the Act and the articles of association. It is also subject to the memorandum of association because director being agents of the company, cannot possess more powers than the company itself.

Article 73 of Table A uses the words ' *subject to regulations ... as may be prescribed by the company in general meeting* '. This gives rise to the question whether the words confer upon shareholders in general meeting a general supervisory power over directors whether in respect of their specific or general powers or both. One view is that art. 73 of Table A confers autonomous power in the hands of the board because the word regulation has the same meaning as the word 'articles'[23] such that if the shareholders want to interfere whether in respect of specific or general powers, they can only do so by altering the articles to take away the powers of the board and this can only be done by special resolution[24].

The opposite view is that shareholders have general supervisory control over the directors[25] with respect to their general as well as their specific powers

---

[22] [1936] 1 Ch 640

[23] *John Shaw & Sons (Salford) Ltd. v. Peter Shaw* [1935] 2 KB 113 per Slesser LJ, at p 143, *Quin & Axtens Ltd. v. Salmon* [1909] AC 442 per Lord Loreburn LC, at p 444.

[24] KW Wedderburn (1968) 31 MLR 688.

[25] Goldberg (1970) 33 Mod LR 177, Blackman (1975) 92 SALJ 286.

without any need to alter the articles such that shareholders may interfere by passage of an ordinary resolution. In the case of *Credit Development Pte.Ltd. v. IMO Pte.Ltd.*[26], a third view was taken. This view endorses the latter view but qualifies it to the extent that the supervisory powers are only in respect of the general power vested in directors under the first limb of art. 73 of Table A.

The preponderance of judicial opinion is against any form of supervisory control by shareholders in general meeting over directors' specific as well as general powers.

1.5.2.2 Malaysian Case Law

In the case of *Dato Mak Kok & Ors v. See Keng Leong & Ors.*[27], the plaintiffs were directors of a public company which had an insurance company as its subsidiary. Some of the plaintiffs were also the directors of the insurance company. Both the articles of association of the public and insurance companies adopted in essence art.73 of Table A. Section 18A of the Insurance Act 1976 provided as follows:

(1) There shall be no change in the control of any Malaysian insurer unless the Director General has given approval in writing for such change.

(2) For the purpose of this section, the expression of 'control' in relation to a Malaysian insurer means the possession directly or indirectly of the power

---

[26] [1993] 2 SLR 370.

[27] (1990) 1 MSCLC 90, 357.

to direct or cause the direction of the management and policy of the insurer.

At a requisitioned extraordinary general meeting, the chairman of the meeting terminated the meeting. Certain shareholders remained behind and continued with the meeting. At the continued meeting, all the plaintiffs were removed as directors and new directors were appointed. The directors who were removed took out an action to restrain the new directors from acting as directors. One of the grounds put forward was that the removal of the plaintiffs as directors contravened s.18A of the Insurance Act 1976 and the corporate veil of the public company and the insurance company ought to be lifted for the purpose of s.18A of the Insurance Act 1976

Zakaria Yatim J applying the principles enunciated in the case of *Automatic Self-Cleansing Machine Filter Syndicate Co. Ltd. v. Cuninghame*[28] and *Gramophone and Typewriter Ltd. v. Stanley*[29] held :

> " The EGM was a meeting of the shareholder of PanGlobal Equities. The proposed resolution was to remove the plaintiff as directors and to replace them with new directors. This did not affect the powers of the plaintiff as directors of PanGlobal Insurance, because as before the EGM of PanGlobal Equities, they are still directors and in control of PanGlobal Insurance. Although PanGlobal Equities owns 99.92% of all the issued share capital in PanGlobal Insurance, PanGlobal Equities cannot interfere with the powers of the directors to control affairs of

[28] Supra note 20.

[29] [1908] 2 KB 89.

PanGlobal Insurance. PanGlobal Equities cannot even impose its will upon the directors of PanGlobal Insurance when the articles of association of the latter have confided to them the control of its affairs."

The above indicates the Malaysian position on the general powers of the management.

1.5.2.3 English case Law

In *Automatic Self -Cleansing Filter Syndicate Co. Ltd. v. Cunninghame*[30] the company had an article similar to article 73 of Table A. A shareholders' meeting was convened and an ordinary resolution was passed directing the directors to carry out a sale of the company's property and to perfect the transaction. The directors refused to carry out the direction as they thought that the sale was improvident and the terms were not favourable to the company. In upholding the stand taken by the directors upon the ground that the directors of the company are not the agents of the shareholders, Collins MR[31] held:

"It has been suggested that this is a mere question of principle and agent, and that it would be an absurd thing if a principle in appointing an agent should in effect appoint a dictator who is to manage him instead of he managing the agent. I think that the analogy does not strictly apply to this case. No doubt for some purposes directors are agents. For whom

[30] Supra note 20.

[31] [1906] 2 Ch. 34 p. 42-43

are they agents? You have, no doubt, in theory and the law one entity, the company, which might be a principal, but you have to go behind that when you look to the particular position of directors. It is by the consensus of all the individuals in the company that these directors become agents and hold their rights as agents."

In the case of *Marshall's Valve Gear Co. Ltd. v. Manning Wardle & Co. Ltd*[32] ., Neville J declined to follow the decision in *Automatic Self Cleansing Filter Syndicate Co. Ltd. v. Cunninghame*[33] on the grounds that in that case, the shareholders sought to interfere by way of an ordinary resolution contrary to the articles and accordingly refused to strike out the action of the company brought by a majority shareholder when the directors refused to sue.

Shortly after the decision of Neville J , Farwell LJ in *Salmon v. Quin & Axtens Ltd.*[34] followed the decision in *Automatic Self-Cleansing Filter Syndicate Co. Ltd. v. Cuninghame*[35] and held that a provision in terms art.73 of Table A did not allow shareholders to interfere with the decisions of directors. Interference can only be justified by the passage of a special resolution to alter the articles. In support of the decision, the decision of Buckley LJ in *Gramophone and Typewriter Ltd. v. Stanley*[36] was cited.

---

[32] [1906] 1 Ch 267.

[33] [1906] 2 Ch 34

[34] [1909] 1 Ch 311.

[35] Supra note 33.

[36] [1908] 2 KB 89

"This court decided not long since, in *Automatic Self -Cleansing Filter Syndicate Co. v. Cunninghame* [1906]2 Ch 34, that even a resolution of a numerical majority at a general meeting of the company cannot impose its will upon the directors when the articles have confided to them the control of the company's affairs. The directors are not servants to obey directions given by the shareholders as individuals; they are not agents appointed by and bound to serve the shareholders as their principals. They are persons who may by the regulations be entrusted with the control of the business, and if so entrusted they can be dispossessed from that control only by the statutory majority which can alter the articles. Directors are not, I think, bound to comply with the directions even if all the corporators are acting as individuals."[37]

Subsequent English cases such as *John Shaw & Sons (Salford) Ltd. v. Shaw*[38] and *Scott v. Scott*[39] have also confirmed the principle that the powers of the board are autonomous , declining to follow the decision in the case of *Marshall's Valve Gear Co. Ltd. v. Manning Wardle & Co. Ltd.*[40] .

In *Breckland Group Holdings Ltd. v. London Suffolk Properties Ltd. & Ors.*,[41] the articles of association vested general powers of management in the board on similar terms as article 73 of Table A. An action was brought without a

---

[37] Ibid, at p. 105

[38] [1935] 2 KB 113

[39] [1943] 1 All ER 582

[40] Supra note 32.

[41] [1989] BCLC 100

resolution of the board which required the affirmative vote of certain directors. A board was subsequently called to adopt and ratify the action. At the same time, attempts were made by the majority shareholders who supported the action to convene a general meeting to adopt the proceedings. It was argued that the outcome of the board meeting really did not matter as it was certain that the general meeting would adopt the action. Harman J. took the opportunity to review the cases discussed above and came to the conclusion that while the decision of Neville J. in *Marshall's Valve Gear Co. Ltd. v. Manning Wardle & Co. Ltd.*[42] had not been expressly overruled, it was in conflict with the majority of cases. Harmen J.[43] held,

> " The principle, as I see it, is that the article confides the management of the business to the directors and in such a case it is not for the general meeting to interfere. It is a fortiori when the shareholders coming together have specifically resolved that some matters be required to have their joint consent and have confided that matter particularly to the directors. That seems to me to reinforce the general proposition which I derive from the authorities cited."

The above seems to indicate the English position on the general powers of management.

---

[42] Supra note 32

[43] Supra note 41, at p 106

1.5.2.4 Australian Case Law

Courts of Australia favour the view that shareholders do not have the power to interfere with decisions of the board of directors acting within their powers. In *Howard Smith Ltd. v. Ampol Petroleum Ltd. & Ors.*[44] , Lord Wilberforce in the Privy Council expressly approved of the decision delivered in *Automatic Self-Cleansing Filter Syndicate Co. Ltd. v. Cuninghame*[45] .

1.5.3 Specific Powers Vested in the Board

Under Table A of the articles of association some of the specific powers vested in the board of directors (in addition to the general powers vested by virtue of article 73 are:-

i. Convening of extraordinary general meetings (art.44);

ii. use of the common seal of the company (art.75 and 96);

iii. borrowing of money and creating securities for any debt, liability or obligation of the company or any third party (art.74);

iv. appointment of managing director and delegating their powers to the managing director, associate director and the secretary (arts.91, 93, 94 and 95);

---

[44] [1974] AC 821.

[45] Supra note 20.

v. recommendation on quantum of dividends (art. 98).

1.5.4 Specific Powers vested in General Meeting

The majority of the powers vested in the body of shareholders in general meeting under Table A are repetitions of the powers which are required to be exercised by the company in a general meeting under the Act. In addition to the provisions of the Act, some of the specific powers vested in the general meeting are:-

i. election of directors in place of those retiring (art.66);

ii. removal of directors, subject to s.128 of the Act (art.69);

iii. declaration of dividend in an amount not exceeding the amount recommended by directors and directions on payments (art. 98 and 104).

1.5.5 Powers conferred by the Act

The legislative intent is that a company and its corporators are free, subject to powers which by the Act are reserved for the general meeting only, to divide powers between the board and the general meeting. Hence, there are only a few instances in which the Act actually confers powers upon directors.

1.5.5.1 Powers vested in board

The following are some of the powers vested in the board of directors under the Act:-

i. appointment of first auditors (s.172(11));

ii. appointment of an approved company auditor to fill a casual vacancy in the office of auditor of the company (s.172(3)) ;

iii. appointment of the company secretary or secretaries (s. 139(3)).

1.5.5.2 Powers vested in general meetings

Powers which are vested in the general meeting under the Act may broadly be divided into two categories. The first category is aimed at controlling potential breaches of fiduciary duties on the part of directors. The second category is aimed at preserving or maintaining the capital of the company.

The following are some of the powers vested in the general meeting:-

1.6 The Company Secretary

Another important officer of the company is the secretary. By virtue of s.139(1) of the Act every company is required to have at least one secretary and s.4 states that the secretary is deemed to be an officer of the company.

The secretary generally has purely ministerial and administrative function and he does not possess any managerial powers as was stated in the case of *Re Maidstone Buildings Provisions Ltd.*[46].

The nature of the secretary's duties varies from company to company. The responsibilities of the secretary are imposed by the Act, the articles or the appointing board of directors.

The courts until recently continued to treat the company secretary as a subordinate servant, without ostensible authority to commit the company by his actions apart from such matters as the engagement of clerical staff. However in modern times the attitude of the courts towards the secretary has changed. In the case of *Panorama Developments (Guildford) Ltd. v. Fidelis Furnishing Fabrics Ltd.*[47] , Lord Denning said that;

> " A company secretary is a much more important person nowadays than he was in 1887[48] . He is an officer of the company with extensive duties and responsibilities. This appears not only in the modern Companies Acts, but also by the role which he plays in the day-to-day business of companies. He is no longer a mere clerk. He regularly makes representations on behalf of the company and enters into contracts on its behalf which come within the day-day running of the companies business. So much so that he may be regarded as though he was held out

[46] (1971) 1 W.L.R. 1085, at 1092

[47] (1971) 2 Q.B. 71, C.A.

[48] That is at the time of the decision in *Barnett, Hoares and Co. v. South London Tramways Co.* (1887) 18 Q.B.D. 815

as having authority to do things on behalf of the company. He is certainly entitled to sign contracts connected with the administrative side of a company's affairs, such as employing staff, and ordering cars and so forth. All such matters now come within the ostensible authority of a company's secretary."

It is arguable, therefore, that the secretary has also graduated as an organ of the company; he is an officer of the company with substantial authority in the administrative sphere and with powers and duties derived directly from the articles and the Act. The powers and duties of the company secretary will be dealt with further in Chapter 2.

1.7 Conclusion

Therefore it can be seen that a company is divided into two constituent parts or organs: the board of directors and the general meeting of members. Wide powers of management are conferred on the board of directors. This is typical of most companies. Accordingly, when the board exercises those powers, its acts are regarded as the acts of the company. In other instances, the acts of the members in a general meeting are considered as the acts of the company. Sometimes the board of directors delegate some of their powers to particular individuals, such as the managing director or the principal executive officer. The acts or state of mind of these individuals may be attributed to the company.

In practice, outsiders rarely deal with the board of directors or the members in general meeting. More often, its relationship with the company involves dealing with its agents or employees. Companies are capable of being bound by the acts of its agents in the same way as natural persons: s.35(4) of the Act. This involves the application of the principles of agency law, in particular the question whether those who purport to act on the company's behalf have the authority to do so. Agency law has several distinct features in its application to companies and which this dissertation will now try to explore.

CHAPTER 2

ULTRA VIRES and AGENCY

2.1 Introduction

In the legal context, a power is the ability to affect a particular change in a given legal relation. In this regard, an individual has the natural legal power to enter into any binding contractual relationship. In contrast, companies have to be endowed with these capabilities and powers by the law. It follows that unlike an individual, a company may only legitimately exercise powers that have been endowed by law.

A company's legal capacity and competence is thus limited because the Act requires a company to state in the memorandum of association the objects of the company. Section 18(1) of the Act sets out the minimum content requirement of the memorandum of association. Amongst others, the memorandum of association was required to contain an objects clause that specifies the range of activities the company was permitted to engage in .

The objects clause was regarded as important from the point of view of the company's shareholders and creditors. They were entitled to expect that the money they invested or lent to the company would be applied in carrying the business listed in the objects clause. The importance of the objects clause was reinforced by the common law doctrine of *ultra vires*. The doctrine provided that any contract made by the company that was not in furtherance of a transaction specified in the objects clause was void.

The role of the *ultra vires* doctrine as explained by the judges was to prevent insidious enlargement of a company's capacity as a result of indiscriminate exercises of powers for

purposes that are neither ancillary or reasonably incidental to the pursuit of authorised objects by rejecting such exercise of powers as being null and void. Although this may result in a very harsh treatment of an outsider who is a *bona fide* purchaser dealing with the company in good faith without notice, this remains necessary if the whole rationale of the *ultra vires* doctrine is to be preserved. In summary, the *ultra vires* doctrine may be expressed in the following sub-rules:

i. a distinction must be drawn between objects and powers ;

ii. an express power is a power that is found in the objects clauses of a memorandum;

iii. an implied power is created by a process of implication on the grounds that a company must necessarily possess powers to do acts for purposes that are either ancillary or reasonably incidental to the pursuit of the authorised objects;

iv. a transaction that is entered into in direct pursuance of an object in the memorandum is valid and binding;

v. a transaction that falls within the scope of an implied or express power is valid and binding only if it is exercised for a purpose ancillary or reasonably incidental to the pursuit of the authorised objects in a company's memorandum.

It can be noted from steps (iii) and (v) that the requirement that a power must be exercised for a purpose ancillary or reasonably incidental to the objects is not only as a touchstone for the implied creation of powers but also as a control mechanism to ensure that powers are exercised within the bounds or capacity of the stated objects.

However, in this age of a complex and fast changing economic environment, a company's dexterity to switch or undertake new business activities may be vital for its survival. Also, businessmen today prefer to operate a group of companies rather than a

sole company in order to take full advantage of limited liability. As a result evasion techniques were introduced by these businessmen.

The other shortcoming of the *ultra vires* doctrine is that it operates harshly on innocent outsiders who constantly run the risk of their transactions with the company being rendered null and void if the purpose of the transaction is outside the scope of the memorandum. As a result, conscious judicial efforts have been made to counter evasion of the *ultra vires* doctrine and also to ameliorate its inherent harshness.

2.2 The Common Law Position before the Rolled Steel case

An illustration of the strict common law application of the *ultra vires* doctrine is provided by *Ashbury Railway Carriage & Iron Co. v. Riche*[1] . The objects of the company, as stated in the memorandum included,

> " to make, and sell, and lend or hire, railway carriages and wagons, and all kinds of railway plant, fittings, machinery, and rolling stock; to carry on the business of mechanical engineers and general contractors".

The directors entered into a contract on behalf of the company for the purpose of a concession to construct a railway. When the company then refused to proceed with the contract the vendor of the concession brought an action against it for breach of contract. The House of Lords held that the construction of railways was not within the objects of the company as stated in the memorandum of association. As the contract was *ultra vires,* it was void and the action against the company failed.

---

[1] (1875) LR 7HL 653

The operation of the *ultra vires* doctrine also extended very broadly. An example of this is *Re Jon Beaufort (London) Ltd.*[2] . A company was incorporated to carry on the business of tailors and manufacturers of clothes and materials. It then decided to manufacture veneered panels, an activity outside its objects. The company ordered coke on the company letterhead which stated that the company was a manufacturer of veneered panels. The supplier of the coke sought to enforce the payment of the debt. He failed because the contract was *ultra vires* ; the company did not have the power to manufacture veneered panels. This was despite the fact that the coke could have been used for the authorised purpose of manufacture of clothes. The coke supplier had actual knowledge that the company was engaged in the manufacture of veneered panels by the information on the company letterhead. He also had constructive notice that such an activity was outside the company's objects. He could have examined the company's memorandum which is a public document.

These cases illustrate the problems which arose from the strict application of the *ultra vires* doctrine. It often resulted in the intention of the parties to a contract being thwarted by application of a technical, unrealistic rule. It enabled a party to a contract to avoid legal obligations or prevented enforcement of legal rights under a contract.

The rationale for this doctrine was that persons dealing with a company were taken to have read the content's of the company's memorandum and articles of association. These are public documents available for inspection. This is known as the doctrine of constructive notice.[3]

---

[2] [1953] Ch 131

[3] *Mahony v. East Holyford Mining Co.* (1875) LR 7 HL 869 p.893

However, it is not realistic to expect all parties dealing with a company to examine the company's memorandum of association. If this were the case, it would impose great inconvenience and would hinder normal business practise.[4]

In order to overcome the problem caused by the doctrine of *ultra vires,* companies drafted the objects clause in the widest possible way. These listed many specific activities and were supplemented by dependent objects which could be construed so as to include any lawful activity.

In the case of *H A Stephenson & Son Ltd. V. Gillanders Arbuthnot & Co*[5] ., the company was incorporated with an independent object of carrying on the business of a product merchant. A dependent object authorised it,

> "to carry on any other business whether manufacturing or otherwise as the company may deem expedient."

Sometime after its incorporation it entered into the business of speculation of jute futures. The High Court held that contracts entered into the course of this business were not *ultra vires* as they were within the dependent object which was widely construed.

Similarly, in *Bell Houses Ltd. v. City Wall Properties Ltd.*[6] , the company was a housing developer. The objects clause of the company's memorandum contained independent objects related to housing development and a dependent object,

> "to carry on any other trade or business whatsoever which can, in the board of directors, be advantageously carried on by the company in connection with or as

---

[4] *Re Jon Beaufort (London) Ltd.* [1953] Ch.131

[5] (1931) 45 CLR

[6] [1966] 2QB 656

ancillary to any of the above business or the general business of the company."

The Court of Appeal held that this dependent object enabled the company to contract to introduce another company to a source of finance. As long as the directors held the honest opinion that a business could be carried on advantageously in connection with the business authorised in the independent objects it was not *ultra vires*.

In the Australian case of *Donohoe v. Stadiums Pty. Ltd*[7] . the company, incorporated in 1914, had an independent object permitting it to run boxing stadiums. In 1988 it commenced trading in listed shares and options. The Supreme Court of New South Wales held that the share trading activities were not *ultra vires* as the company had a dependent object similar to that in the *Bell Houses Ltd.*[8] case.

Where the memorandum contains an objects clause it will state that the company has the object of conducting particular businesses. To carry on this business the company must have certain powers which are incidental to the attainment of its objects. The exercise of such powers is not ultra vires provided that they are incidental to one of the company's independent objects. However, in some cases a company may seek to exercise a power, incidental to its main object but for an extraneous purpose. In the case of *Attorney General v. Great Eastern Railway Co*[9] . it has been held that the court will generally permit a company to operate with wide powers if they are incidental to either its main or independent objects.

The practise has also developed of concluding a company's objects clause with a declaration that each of the specified objects and powers are to be interpreted

---

[7] (1993) 11 ACLC 190

[8] [1966] 2QB 656

[9] (1880) 5 App. Cas. 473

independently of another. In the case of *Re Introductions Ltd.*[10] , the company's objects clause concluded with the following statement:

> " It is hereby expressly declared that each of the preceding sub-clauses shall be construed independently of and shall be in no way limited by reference to any other sub-clause and that the objects set out in each sub-clause are independent objects of the company."

In that case the company's main object was to provide services for tourists visiting Britain. It also had a dependent object authorising the company to carry on any other business which in the opinion of the board could be carried on in connection with its main objects The objects clause also included the power to borrow money.

Several years after its incorporation the company ceased its tourist business and carried on a pig-breeding business. In furtherance of that business it borrowed money from its bank. The bank was aware of its objects clause and the company's new business. The court held that loan from the bank was *ultra vires*. The power to borrow could not converted into an independent object merely because of a provision to that effect in the memorandum.

The decision in *Re Introduction*[11] was criticised in *Re Tivoli Freeholds Ltd.*[12] , on the basis that the power to borrow, whilst not incidental to the company's main object, was incidental to its dependent object of carrying on any other business which would be carried on in connection with its main objects. Despite this criticism, prudent lenders

---

[10] [1969] 1 All ER 887

[11] [1969] 1 All ER 887

[12] [1972] VR 445

often, in cases of doubt as to the extent of the object, require a company to alter its objects expressly to give it the required authority.

Drafting techniques were employed by the business community to produce results that would obfuscate the clear distinction between objects and powers. For example, it is widespread drafting technique to enumerate the objects clause in the memorandum at great length so as to render a company's limited capacity almost limitless. The courts initially responded by construing only one of these objects as the main object and the rest only as ancillary powers.

This caused the business community to insert what is now known as the *Cotman v. Brougham*[13] clause which is an express declaration in the objects clause to the effect that each of the specified objects or powers should be deemed to be independent and not ancillary or subordinate to any other objects. The House of Lords in the case of *Cotman v.Brougham* approved of such a clause and Lord Parker justified the result on the ground that :

> "...a person who deals with a company is entitled to assume that a company can do everything which it is expressly authorised to do by its memorandum of association ...."

Subsequently, it was felt that if the effect of such a clause remained unchecked it would seriously undermine the *ultra vires* doctrine. Several judges began to express the view that where objects were really mere powers they must be treated as powers notwithstanding the presence of a separate objects clause[14] .

---

[13] (1918) A.C. 514

[14] See for example Buckley's L.J. judgement in *Re Horsley & Wright [1982] 1 Ch. 442 at p.448*

This view was also affirmed by Slade L.J. in his judgment in the case of *Rolled Steel (Holdings) Ltd. v. British Steel Corporation*[15] where he accepted the argument that full force must be given to the *Cotman v. Brougham* clause unless the power in question is by nature incapable of constituting a substantive object. Clearly, an independent clause would not elevate what is essentially a power into an object.

Further, Slade L.J. in the *Rolled Steel* case[16] subjected the *Cotman v. Brougham* clause to one more restriction. He took the view that a construction of the memorandum as a whole might show that the sub-clause, whether containing a power or an object, was intended as an ancillary power only.

In the case of *Re Horsley & Weight Ltd*[17] ., Buckley L.J. has justified this need for implied powers in the following words:

> "...for it is the practical need to imply the power in order to enable the company effectively to pursue its authorised objects which justifies the implication of the powers."

Gower states in his text that the strict ultra vires rule is also to be applied reasonably so that whatever is incidental to the objects expressly authorised by the memorandum or statute, unless expressly prohibited, will be *intra vires*[18] .

The modern expression of this rule is that an exercise of power is *intra vires* if it is ancillary or reasonably incidental to the pursuit of an authorised object[19] .

---

[15] (1984) B.C.L.C.466

[16] (1984) B.C.L.C.466

[17] [1982] Ch. 442

[18] Gower's Principles of Modern Company Law (4th Edition) 1979 p.165

[19] per Buckley L.J. in *Re Horsley & Wright Ltd. (1982) Ch.442 at p.448*

It follows that a distinction between objects and powers is vital. The reason is that true objects are in substance well-defined business activities or purposes which are capable of being pursued in isolation as the sole activity of the company. Such objects are therefore truly capable of defining and limiting a company's capacity. Powers, on the other hand, are mere abilities which may be exercised for any purpose including those purposes that are neither ancillary nor incidental to the pursuit of authorised objects.

It is hence fundamental to the *ultra vires* doctrine that a distinction be maintained between objects and powers.

The above discussions reveal the extent to which attempts have been made to evade the *ultra vires* rule and how judges have tried to contain these efforts.

2.2.2 THE ROLLED STEEL ULTRA VIRES DOCTRINE

In the light of these controversies, the Court of Appeal judgement in the *Rolled Steel* case[20] deserves close scrutiny , especially as the judgement has been described as an attempt by Slade L.J. to remodel the *ultra vires* doctrine.

The facts of the case are that there are four companies involved in a chain of indebtedness. One SSS Ltd. owed some 860,000 Pounds (Sterling) to a C Ltd. On the other hand, SSS Ltd. was a creditor of Rolled Steel Products (Holding) Ltd. (hereinafter referred to as 'RSP') and had lent to RSP a sum of 400,000 Pounds (Sterling). However both SSS Ltd. and RSP were owned and controlled by the Shenkman family.

---

20 B.C.L.C. 466

Subsequently , C Ltd. was taken over by the British Steel Corporation (hereinafter referred to as 'BSC') which continued to press SSS Ltd. for the repayment of its debts to C Ltd..

To ensure that SSS Ltd. would finally pay its debt, BSC pressed for a personal guarantee by Mr. Shenkman as well as a company guarantee by RSP which owned sufficient assets to meet the debt.

Although Mr. Shenkman acceded to the demand , RSP could not readily do so as the payment under the guarantee by RSP to BSC which was in excess of RSP's debt of 400,000 pounds to SSS Ltd. might subsequently have been attacked as a fraudulent preference over RSP's creditors and perhaps even as an act of misfeasance on the part of the directors.

The solution to this problem was that C Ltd. would lend a further 401,448 Pounds (Sterling) to RSP before RSP issued the guarantee to BSC. This money would then be used to extinguish RSP's debt to SSS Ltd. And SSS Ltd. would, in turn, use the same partially to reduce its debt of 860,000 Pounds (Sterling) to C Ltd. Having transferred , in effect , a portion of SSS Ltd.'s debt to RSP, RSP would then agree to guarantee the balance of SSS Ltd.'s debt to C Ltd. and failing that , RSP was to issue a debenture in favour of C Ltd..

A disquieting feature of the scheme was that Mr.Shenkman had earlier personally guaranteed SSS Ltd.'s indebtedness to C Ltd. . The transfer of a portion of SSS Ltd. debt to RSP served to benefit him as it would reduce his liability under his guarantee. In contravention of Article 17 of RSP's Articles of Association , Mr.Shenkman

subsequently approved of the scheme without any declaration of his self-interest in this series of transactions.

On 25 March 1975 , RSP brought an action against BSC, the receiver , the trustees in bankruptcy of Mr.Shenkman and his father on the following grounds:-

i) neither the guarantee nor the debenture was the deed of RSP, because it was not duly executed by RSP. The reason was that Mr.Shenkman was personally interested in the arrangements and because he had not declared his interest in accordance with article 17 and 18(a) of the Articles of Association of RSP he was not entitled to guarantee the debenture. In short, there had been no proper quorum of directors voting on the resolution;

ii) if contrary to the plaintiff's submission, the guarantee and the debenture were the deeds of RSP, each of them was *ultra vires* and void because the arrangements were made not for the purposes or benefit of Mr.Shenkman;

iii) if contrary to the plaintiff's submission, the guarantee and debenture were the deeds of RSP and were *intra vires* RSP, the directors were acting in breach of their fiduciary duties because these transactions were entered into in bad faith and not for the purposes of RSP. It followed that BSC and the receiver , having received the monies with actual or constructive knowledge of this breach, took them as constructive trustees.

In defence, the defendants sought to rely on the *rule in Turquand's* case in that although the resolution was defective the defendants were entitled to rely on it as a formally valid resolution. They also argued that the shareholders by having unanimously consented to

the execution of the guarantee and debenture ratified and made binding the transaction in question.

With regard to the shareholder's consent point, the court and in particular Slade L.J. took the view that as this argument was raised after the close of evidence, it came too late to be heard. Slade L.J. also confirmed an important factual finding that C Ltd. and BSC knew that the guarantee and the debentures were not entered into by RSP for any purpose of RSP, but were gratuitous disposition of the property of RSP and were entered into by RSP for the benefit of SSS Ltd. and Mr.Shenkan personally.

This knowledge was imputed to C Ltd. and BSC because legal advice given to RSP's solicitor that the proposed transactions were probably *ultra vires* and constituted a misfeasance by its directors was reported to the head of the legal services department of C Ltd..

The finding of this knowledge on the part of the defendants was fatal to their appeals for the following reasons:-

a) if the transactions were found to be *ultra vires*, they could not rely on the rule that as bona fide purchasers without notice the transactions remained binding;

b) if the transactions were found to be *intra vires* , they alternatively constituted a breach of director's fiduciary duties. The same transactions could be set aside at the instance of the company and the directors would be liable as constructive trustees because they had assisted with knowledge in a breach of trust;

c) if the transactions were held to be *intra vires* and to be treated as instances of directors exceeding their authority as agents , this knowledge on the part of the defendants would disentitle them from relying on the doctrine of apparent

authority to validate the transactions.

Slade L.J.'s efforts to answer this question in effect amounted to a restructuring of the *ultra vires* doctrine, resulting in a modified new model *ultra vires* doctrine being introduced.

In summary, the following were held by Slade L.J. :-

1) that a sharp distinction must be maintained between objects and powers. It follows that powers ought not to be inserted in a company's memorandum and the exercise of any implied or express powers should also be controlled so that a company is treated as having implied powers only to do acts for purposes which are reasonably incidental to the attainment or pursuit of any of its express objects[21];
2) following from the above, the proposition that once a clause is capable of subsisting as an independent object of the company it cannot be *ultra vires* for it is by definition something which the company is formed to do and so must be *intra vires*;
3) he took the view that even if a sub- clause might exist as a substantive object, a construction of the memorandum as a whole might show that it was intended to constitute an ancillary power only. The presence of a *Cotman v.Brougham* clause should not elevate what were essentially powers into objects.
   However, Slade L.J. did express the view that wherever possible the *Cotman v. Brougham* clause be granted its full impact .

[21] Supra, note 20 at p. 500

4) Since the sub-clause was in the nature of a power, the view that strict logic might require that any exercise of such a power whether implied or express would be beyond the company's capacity if the resultant transactions were in fact performed for purposes other than those of its incorporation.

However, Slade L.J. modified rule 4 above on the ground that the practical difficulties resulting from such a conclusion for persons dealing with a company carrying on a business authorised by the memorandum would be intolerable. To solve the problem, Slade L.J. relied on Buckley's judgement in *Re David Payne & Co.Ltd.*[22] , as stating the proper alternative approach. Under this approach, an act that is beyond the objects clause would not be regarded as ultra vires. It follows that the act would become voidable but not void. Such an act would instead be treated as an act of impropriety on the part of the directors who have exercised the powers in question. Since this only raises questions of equity between the directors and the shareholders it does not affect the legal quality of the act vis-a-vis the outsider without notice of the impropriety.

In Slade L.J.'s view, directors' authority as agents is limited by the implied condition that they must exercise their powers only for the purposes of the company and therefore any such express restrictions found in the sub-clauses in a memorandum merely reinforced such a condition. Slade L.J. was therefore suggesting that every general power contained in a company's memorandum was subject to the express or implied restriction that it must be exercised for the purposes of the company. Thus, every exercise of power outside the condition ought not to be treated as *ultra vires* but as an instance of directors exceeding their authority. Slade L.J. then put forward the proposition that an outsider acting without

[22] [1904] 2 CH 608

notice of the impropriety of the transaction in question may invoke the independent "indoor management rule" and the agency doctrine of apparent authority in their favour.

This brings us to the end of Slade L.J.'s valiant efforts to remodel the *ultra vires* doctrine affecting ancillary 'objects' and 'powers' .

At this juncture, it is useful to recall that the basic justification for the concept of limited capacity is that it protects shareholders and existing creditors by rejecting as null and void transactions between the company and the outsider if the purpose of that transaction is outside the scope of the memorandum. It follows that an outsider whose transaction with the company is now being challenged as *ultra vires* runs the risk of the transaction being held null and void. Theoretically, this system of protection is thought to be a fair system because a company's limited capacity is ascertainable by its memorandum which is a constitutional document of the company freely available for inspection.

However, commercial realities have shown that the system may work oppressively for the following reasons:-

1) businessmen have neither the time nor the resources to study a company's memorandum in order to acquaint themselves with its legal capacity;
2) they may not appreciate the significance of the distinction between objects and powers.
3) it is also extremely unjust that the company which has solicited the interest of the outsider in the transaction now, for its own reasons, turns around and invokes the *ultra vires* doctrine arguing that the transaction should be set aside as being null and void.

2.3 Should Agency Principles Be Used In Place Of The Strict *Ultra Vires* Doctrine

Slade L.J. in the Rolled Steel case believed that the anomalous *ultra vires* rule[23] could be explained by using the agency principles. In his opinion, an outsider was entitled to rely on the fact that as a general rule, a company incorporated under the Companies Act held out to its directors as having ostensible authority to do on its behalf anything which its memorandum of association, expressly or by implication gave the company capacity to do[24] It followed that if a sub-clause in the memorandum authorised a company to borrow for the purposes of the company, its directors would have the power to do so, as long as the outsider had no notice of their ulterior motive to use the borrowed money for a 'foreign' purpose. Since the company through its memorandum held out its directors as having the apparent authority to borrow, then not only is the *ultra vires* issue pre-empted but the express condition that the borrowing must be done for the purposes of the company would also be construed not as limiting a company's capacity but simply as limiting the authorities of the director[25] . Although the outsider had constructive knowledge of the memorandum including any condition that was attached to the sub-clause, he nevertheless had no notice of the breach of the condition because he was entitled to assume that its directors were properly exercising such powers for the purposes of the company as set out in the memorandum[26]

In the opinion of Slade L.J., three factors actually operated to legitimize this particular assumption.

---

[23] See Baxter, supra, note 26 at p. 280

[24] Supra, note 20, at p.507

[25] Ibid, at p. 507

The first factor has already been stated, that is, a company holds out its directors as having apparent authority to bind the company to any transaction which falls within the powers expressly or impliedly conferred on it by its memorandum of association[27] .

The second factor is based upon policy considerations and is reflected in the rule that an outsider is under no duty to investigate and inquire into the purpose behind a transaction. In this connection Slade L.J. cited Buckley J.'s words in *Re David Payne & Co. Ltd.*[28] that:-

> "A corporation, every time it wants to borrow, cannot be called upon by the lender to expose all its affairs, so that the lender can say, before I lend you anything, I must investigate how you carry on your business, and I must know why you want the money, and how you apply it, and when you have it I must see you apply it in the right way."

It is impossible to work on such a principle.

The third factor is that an outsider is entitled to assume on the authority of the principle stated in the case of *Royal British Bank v. Turquand*[29] that the directors of the borrowing company were acting properly and regularly in the internal management of its affairs and were borrowing for the purposes of the company's business.[30]

---

[26] Ibid., at p. 508

[27] Ibid., at p. 507

[28] [1904] 2 Ch. 608, 613

[29] (1856) 6 E&B 327; 119ER 886

[30] Supra note 20, at p.504

In summary, the gist of Slade L.J.'s judgement is that any act that falls within the scope of a company's powers is *intra vires*. From now on the strict logic of the *ultra vires* doctrine will continue to have impact only in cases where the act in question does not even, to begin with, fall within the scope of the company's powers.

An interesting comment on this development was expressed by *Clark* in the following words[31]:

> " On this narrow view, few activities will fall outside the corporate capacity of the modern limited company. With the standard multifarious list of objects/powers, a *Cotman v. Brougham* and a *Bell Houses* sub-clause[32] , a company's contractual capacity will be close to that of a natural person. By the decision in Rolled Steel[33] case the court has abandoned the ultra vires doctrine as the appropriate vehicle for implementing the prime policy aim of protecting shareholders and creditors. In order to strike down an unreasonable depletion of corporate assets, such as in *Rolled Steel*[34],*Re Introduction*[35] and *Re David Payne*[36] , other means - including breach of duty and the law of agency - will be used."

---

[31] See Clark, "Ultra Vires after Rolled Steel Products", (1985) 6 Co. Law 155, 158

[32] The English Bell Houses clause (*Bell Houses Ltd .v. City Wall Properties,* [1966] 2QB. 656) authorised the company " to carry on any other trade or business whatsoever which can, in the opinion of the board of directors, be advantageously carried on by the company in connection with or ancillary to any of the objects of the company." This as noted by Ford imposes a subjective test of honest belief on the directors. See H.A.J. Ford, Principles of Company Law, (1982, 3rd Ed.) p. 96.

[33] (1984) B.C.L.C. 446

[34] Supra note 70

[35] (1970) 5 App Cas 473, H.L.

[36] (1904) 2 Ch. 608 ,613

2.4 The English Position on the Doctrine of Ultra Vires

In England, it was long recognised that the strict *ultra vires* doctrine in relation to companies should be abolished.

Section 9 of the European Communities Act 1972, later re-enacted as section 35 of the Companies Act 1985 attempted to dispose of all the problems posed in short sub-sections, the first of which provided that, in favour of a person dealing with a company in good faith, any transaction decided on by the directors should be deemed to be within the capacity of the company and free from any limitations under the memorandum and articles on the directors' powers, and the second of which relieved the other party of any obligation to inquire about those matters.

Although this was a considerable step forward it was widely criticised for various reasons. It was said that it only covered '*transactions decided by the directors*', and protected only a third party '*dealing with the company in good faith*' and it did nothing to protect the company against invocation of *ultra vires* by the other party.

2.4.1 The Companies Act 1989 -

Virtual abolition of ultra *vires doctrine*

In 1989, a further amendment to the Companies Act made an attempt to remove the consequences of exceeding any limitations on a company's capacity without actually admitting that it had full capacity. It did this by substituting for the original section 35 of the 1985 Act new sections 35, 35A and 35B.

Subsection (1) of the new section 35 of the Companies Act 1989 reads as follows:-

> "The validity of an act done by a company shall not be called into question on the ground of lack of capacity by reason of anything in the company's memorandum."

This is an improvement of the former section 35(1), as it deals directly with the effects of lack of capacity instead of attempting, to deal in the same sub-section with acts in excess of directors' powers. It omits the former words "*in favour of a person dealing with a company*" and thereby does not merely remove the uncertainties flowing from "*dealing with*" but makes it clear that neither the company nor a third party can any longer invoke the strict *ultra vires.* Had the section stopped there the only question that would have remained was whether the acts done failed to bind the company because those acting for it had acted outside their actual or apparent authority.

2.4.2 Lack of authority and constructive notice

These two matters were dealt with by sections 35A , 35B and section 711 of the Companies Act 1989.

Section 35A sub-section (1) provides:-

> "In favour of a person dealing with a company in good faith, the power of the board of directors to bind the company, or authorise others to do so, shall be deemed to be free of any limitations under the company's constitution."

This, too, is an improvement on the wording of the former section 35 in that it omits the restriction to "transactions decided on by the directors" and thus recognises that many

transactions will be decided upon by executive officers appointed by the board of directors.

However this section is not free from difficulties. The first difficulty is that, the Companies Act 1989 has never defined what the powers of the directors are. This is left to the memorandum and articles of association.

A more serious objection is that section 35A(1) of the Companies Act 1989 fails to afford any protection when the third party has dealt with another organ of the company for example the members in the general meeting to whom there may have been certain powers awarded under the company's constitution.

The section however went on to add some qualifications:-

Subsection (2) provides:

> " A member of the company may bring proceedings to restrain the doing of an act which for subsection (1) would be beyond the company's capacity; but no such proceedings shall lie in respect of an act done in fulfilment of a legal obligation arising from a previous act of the company."

A second qualification was added by subsection (3), which provides that:

> "It remains the duty of the directors to observe any limitation on their powers flowing from the company's memorandum and any action by the directors which, but for subsection (1), would be beyond the company's capacity may only be ratified by the company by a special resolution. A resolution ratifying such action

shall not affect any liability incurred by the directors or any other person; relief from any such liability must be agreed to separately by special resolution."

This subsection was included because of the English Government's declared policy to abolish *ultra vires* in relation to external relations but, so far as possible, to maintain the status quo for internal relations between the company and its directors.

Subsection (1) of section 35A of the Companies Act 1989 retains the expressions "*dealing with the company*" and "*in good faith*" which caused some difficulty in the earlier version of section 35. However, subsection(2) of the new section35A gives help in the interpretation.

It provides:

For this purpose-

a) a person "deals with" a company if he is a party to any transaction or any act to which the company is a party;

b) a person shall not be regarded as acting in bad faith by reason only of his knowing that an act is beyond the powers of the directors under the company's constitution; and

c) a person shall be deemed to have acted in good faith unless the contrary is proved.

Subsection (2)(a) provides a straightforward test of whether a person is "*dealing with a company*". He will be, so long as he is a party to a transaction or an act to which the company is also a party. Further, knowledge is itself not conclusive evidence that the party acted in bad faith.

Section 35A(3) of the Companies Act 1989 makes it clear that "*any limitation under the company's constitution*" includes not only a limitation in the memorandum and articles but also one deriving from an agreement or resolution of the members even if it does not formally alter the memorandum or articles themselves.

Section 35B of the Companies Act 1989 provides that:

> " A party to a transaction with a company is not bound to inquire as to whether it is permitted by the company's memorandum or as to any limitation on the powers of the board of directors to bind the company or authorise others to do so."

On its own this adds little to what is already implied by section 35 and 35A and stops far short of totally abolishing the doctrine that those having dealings with a company are deemed to have notice of its public documents. That further step, is however, taken by the new section 711(1) of the Companies Act 1989 which provides that :

> " A person shall not be taken to have notice of any matter merely because of its being disclosed in any document kept by the registrar of companies (and thus available for inspection) or made available by the company for inspection."

The result of this is that those dealing with the company are no longer deemed to have notice of the contents of any document merely because it is one of the company's documents available for inspection at the Registrar of Companies or the company's registered office.

Subsection (1) is, however, qualified by subsection (2) which reads :

"This does not effect the question whether a person is affected by notice of any matter by reason of a failure to make such inquires as ought reasonably be mad."

Gower[37] states in his text that at first glance this might appear to diminish the protection afforded by section 35A of the Companies Act 1989 to a person dealing with a company in good faith. However this is not so. Under section 35A of the Companies Act 1989, in favour of such a person " *the power of the board of directors to bind the company or authorise the others to do so*" is deemed to be free of any limitation and he is not regarded as acting in bad faith. " by reason only of his knowing that an act is beyond the powers of the directors." In this case, section 711A of the Companies Act 1989 is relevant only in situations where section 35A of the same Act does not protect him because it is not the board of directors that has exceeded its powers but the officer of the company through whom he dealt with the company. Here, it is not suggested that a failure to make such inquires that ought to made may not be evidence of bad faith; however if he has deliberately decided not to make inquires knowing that, if he does, it is likely to confirm his suspicions that the board is exceeding its powers, that may be treated as equivalent to actual knowledge and, in consequence, as probable bad faith.

Gower further states that negligent failure to make further inquires cannot, in itself, constitute bad faith.

---

[37] Gower's Principles of Modern Company Law (4th Edition) p.181

2.4.3 Transactions involving Directors

The new section 322A of the Companies Act 1989 constitutes an important qualification to the new sections 35 and 35A. It applies where the transaction exceeds a limitation on the powers of the board of directors under the company's constitution and the other parties include a director of the company or the holding company, or a person connected with such a director, or a company with which such a director is associated. In such circumstances the transaction is voidable at the instance of the company and, whether or not it is avoided, such parties and any director who authorised the transaction, knowing that it exceeded the board's powers, are liable to account to the company for any gains they make and to indemnify the company against any loss it suffers.

The objective of the foregoing statutory changes was as Gower points out "to draw the sting of the *ultra vires"* and constructive notice doctrines, thus improving the position of those who dealt with the company externally, while making as few alterations as possible to the position as between the company and its members, directors and its other agents.

2.5 The Malaysian Position on the Doctrine of Ultra Vires

The Companies Act 1965 (hereinafter referred to as the 'Act') was drafted by using the Uniform Companies Act of Australia as it's main model. Section 20 of the Act which is derived from s.20 of the Australian Uniform Companies Act 1961 made important changes to common law doctrine of ultra vires in Malaysia. It releases an outsider who is contracting with the company from any adverse application of the doctrine.

Before analysing s.20 of the Act, reference will be made first to s.18 and s.19 of the Act. Section 18 of the Act requires every company to have an objects clause in its' Memorandum of Association. In addition to the powers given to the company in the objects clause, the company has all the powers stated in s.19 of the Act, which is :-

a) power to make donations for patriotic or for charitable purposes (s.19 (1)(a));

b) power to transact any lawful business in aid of Malaysia in the prosecution of any war or hostilities in which Malaysia is engaged (s.19(1) (b)); and

c) unless expressly excluded or modified by the memorandum or articles, the powers set forth in the Third Schedule but the powers of a company which has by the license of the Minister pursuant to s.24 been registered without the word "Berhad" or pursuant to any corresponding previous written law been registered without the addition of the word "Limited" to its name shall not include any of the powers set forth in the Third Schedule unless expressly included in the memorandum or articles with the approval in writing of the Minister (s. 19(1)(c)).

2.5.1 Section 20 of the Act

The common law principle that an act of the company which is ultra vires does not bind the company to the outsider or vice-versa is set aside by s.20(1) of the Act. As a result, an outsider can sue or be sued under a contract entered into by the company which has exceeded its powers as stated in the objects clause. This can be illustrated in the case of *Pamaran Holdings Sdn.Bhd. v. Ganda Holdings Bhd.*[38] . In this case, by an outsider attempted to release himself from the terms of a contract with a company by raising the

[38] (1988) 1 MSCLC 90, 165

doctrine of ultra vires as a defence. He failed because s.20 of the Act had removed the application of the doctrine between the company and an outsider.

The Act is silent on whether the doctrine of constructive notice of the public documents of the company, like the Memorandum or Articles of Association will be applicable to s.20 of the Act. However, it may be presumed that the doctrine of constructive notice will not be applicable to s.20 of the Act, because if it is, it will defeat the very purpose of s.20 of the Act.

Section 20 of the Act was also applied in the case of *Public Bank Bhd. v. Metro Construction Sdn. Bhd.*[39] . In this case M Bhd. had created two charges over a piece of land as security for a loan given by Bank P to another company, that is T Bhd.. T Bhd. has no relationship with M Bhd.. Bank P foreclosed on the land.It was argued that the charges were created not for the benefit of M Bhd. but for the benefit of T Bhd. and further that the directors of M Bhd. had acted beyond the powers given to them by the articles. Also, it was alleged that two of the directors of M Bhd. had committed fraud. However, there was no allegation made that Bank P had knowledge of the alleged fraud. The memorandum of association of M Bhd. allowed the company to borrow money and create a charge for a legally valid reason. The articles of association of the company allowed the directors of the company to borrow money for the company. Justice Lim Beng Choon held that both charges were within the powers given by the objects clause of the company. The judge relied on the decision of In R*e David Payne & Co.*[40] and the

---

[39] [1991] 3 MLJ 56

[40] [1904] 2 Ch 608.

case *Rolled Steel Products (Holdings) Ltd. v. British Steel Corporation & Ors.*[41] and held that the loan and the charge was valid because if a company was allowed to borrow money for its business, the lender is not required to inquire the purpose for which the money is going to be used. The judge also relied on s.20 of the Act and stated that even though the company acted ultra vires its memorandum, the transaction can still be valid by virtue of s.20 of the Act.

A pertinent point is whether an act which is ultra vies the article can be saved by s.20 of the Act. Section 20 (1) of the Act states:

> " No act or purported act of the company ... and no conveyance or transfer of property, whether real or personal, to or by a company shall be invalid by reason only of the fact that the company was without capacity or power to do the act or to execute or take the conveyance or transfer."

It is about the powers of the company as stated in the memorandum. It is not about the authority of the directors or the officers of the company as stated in the articles of association. The authority of directors or officers and how far they can bind the company is usually stated in the articles of association. At common law, an outsider is taken to have constructive notice of the contents of the memorandum and articles of association of the company. If an act of an agent of a company is clearly outside the articles of association, the outsider is said to have constructive notice of the abuse of power. The fact that the outsider did not actually read the article is immaterial. The act though not ultra vires under s.20 of the Act, can be avoided by the company under the law of agency.

---

[41] Supra note 16

In the case of *Public Bank Bhd. v. Metro Construction Sdn. Bhd.*[42] , the judge chose to combine the two issues, that is, the capacity of the company and the authority of its organs and agents. This, confused what was painstakingly untwined by the Court of Appeal in the *Rolled Steel* case. The judge first held that the two directors had ostensible or apparent, if not actual authority to execute the charges. However, he still had to address the improper purpose argument, that is, the directors could not borrow money if the borrowed money was not used for the purposes of the company.

He went on to cite the case of *Cotman v. Brougham*[43] and the case of *Re Introductions*[44] and held that where a company has a general power to borrow money for the purposes of its business, a lender in not bound to enquire into the purpose for which the money is to be applied.

Thus, under normal circumstances a third party need not enquire and if he does not and is ignorant of the purposes, the transaction is binding on the company.

The issue then is what is the basis for this principle, ultra vires or agency? In *Re Introduction*[45], the basis was ultra vires until it was remodelled as agency by the Court of Appeal in the *Rolled Steel* case.[46]

---

[42] [1991] 3 MLJ 56

[43] Supra note 13

[44] Supra note 11

[45] Supra note 11

[46] Supra note 16

Lim Beng Choon J. in the *Metro* case[47] quoted the *David Payne's*[48] case as authority for the two propositions : (1) that where there is a power to borrow for the company's business and the borrowing is made otherwise than for those purposes, the borrowing is not void as being ultra vires; and (2) a third party is not put on notice by an express requirement that the power is only exerciseable for the purposes of the company's business.

Therefore though he seems to have avoided giving a definite answer pertaining to whether it is ultra vires or agency, by holding that, whatever the case, the transactions were binding as the party had no knowledge of the improper purpose. The fact that he has quoted with approval the two propositions goes to show that this case gives judicial support for both the propositions.

Therefore the narrow view of ultra vires, that is, a transaction within the company's powers but for unauthorised objects would not be ultra vires and would not fall within the scope of s.20 of the Act seems to be good law in Malaysia.[49]

Another case which is similar to the facts of *Public Bank Bhd.. v. Metro Construction Sdn. Bhd.*[50] and was decided likewise is the case of *Executive Aids Sdn. Bhd. v. Kuala Lumpur Finance Bhd.*[51] .

Even though s.20 (1) of the Act has set aside the doctrine ultra vires as far as the outsider

---

[47] Supra note 42

[48] Supra note 22

[49] Ultra Vires and Agency – Untwined and Entwined? Public Bank Bhd. v. Metro Construction Sdn.Bhd. by Patricia Ong – Wee GS (1992) 2MLJ p cv

[50] Supra note 42

[51] {1992} 1 MLJ 89

is considered, there are still some effects of the common law doctrine applicable in Malaysia.

Firstly, s.20 (2)(a) of the Act states that an ultra vires act may be restrained before it is fully performed by a member or a debenture holder secured by a floating charge. A discussion of s.20(2)(a) of the Act is incomplete unless reference is also made to s.20 (3)of the Act.

Section 20 (3) of the Act reads as follows:

> " If the unauthorised act, conveyance or transfer sought to be restrained in any proceedings under subsection (2) (a) is being or is to be performed or made pursuant to any contract to which the company is a party, the court may, if all the parties to the contract are parties to the proceedings and if the court deems it to be just and equitable, set-aside and restrain the performance of the contract and may allow to the company or to the parties to the contract (as the case requires) compensation for the loss or damage sustained by either of them which may result from the action of the court in setting aside and restraining the performance of the contract but anticipated profits to be derived from the performance of the contract shall not be awarded by the Court as a loss or damage sustained."

Clearly the intention of s.20 (3) of the Act is to protect both the company and the innocent outsider or the third party from the effects of s.20 (2) (a) of the Act. Where an executory ultra vires transaction is restrained by the court under s.20 (2) (a) both the company and the outsider may suffer loss as expenses may have been incurred in anticipation of the contract being performed by both parties. Section 20 (3) of the Act gives the court a wide discretion to order compensation for either party to the transaction

in the event the court grants a restraining order or an injunctive relief.[52] It is to be highlighted however that the courts power, although couched in wide terms, does not extend to awarding damages for loss of anticipated profits.

The first point to note from s.20 (2) (a) of the Act is that the right to restrain is also given to a debenture holder under a floating charge, a peculiarity of the Malaysian provision. The second point is that the right to restrain arises even though a binding relationship has arisen between the company and the outsider or third party. However, the right is only available where the transaction is executory and not fully performed. The third point to note is that the company itself cannot be an applicant under s.20 (2) (a) of the Act. It is debarred by s.20 (1) of the Act from asserting ultra vires. The fourth point is that the member or debenture holder under a floating charge cannot seek any injunctive relief against the outsider or third party. This is because by virtue of s.20 (1) of the Act the ultra vires doctrine has been abolished as between the company and the outsider. The member or debenture holder must therefore seek to restrain the company from executing the ultra vires act. The fourth point was stressed by Street J. in the instructive case of *Hawkesbury Development Co. Ltd. v. Landmark Finance Pty. Ltd.*[53]

Secondly, s.20 (2) (b) of the Act states that the issue of a company's lack of capacity may be raised in any action by the company or any member against any present or former officers of the company. This may be an action to restrain an officer from causing the

---

[52] Obviously the outsider or third party must be a party before the court before it can grant it an order in its favour. As to procedural details by which the outsider may be made a party see Balan and Talat Mahmood, "Doktrin Ultra Vires dan Sekyen 20 Akta Syarikat 1965", an article about to be published in the Journal of Malaysian & Comparative Law (JMCL) Vol.23.

[53] (1970) 92 WN (NSW) 199

company to act in a manner that is unauthorised by its memorandum of association or an action against an officer in respect of his breach of duty in causing the company to do an ultra vires act.

Thirdly, the fact that a company has acted beyond its capacity may be relied upon in any petition by the Minister to have the company wound-up.

Fourthly, the case of *Ashbury Railway Carriage & Iron Co. v. Riche*[54] it was stated that if a transaction is ultra vires, it may not be made intra vires even by the unanimous assent of the members. In Malaysia, there is no necessity for ratification in order to make an ultra vires transaction binding; because it is binding by virtue of s.20(1) of the Act. However, the principle an ultra vires act cannot be made intra vires even with the unanimous consent of the members still remains. This means a member may still try to restrain an ultra vires act even though he had previously consented to it. However, the court will take into consideration the previous consent of the member before it exercises its discretion to restrain the act.

Finally, s.20 of the Act has no application to foreign companies as the section refers to companies and not corporations. S.4 of the Act state that a company refers to a company incorporated under the Act.

---

[54] Supra note 1

2.6 The Australian Position on the Doctrine of *Ultra Vires*

Prior to 1st January 1984, the memorandum of every company in Australia had to contain an objects clause. S.117(2) of the Australian Corporations Act 1984 (hereinafter referred to as "the Law") eliminated this requirement. Companies incorporated after 1 January 1984 have had a choice whether or not to include an objects clause in the memoranda. Further, companies, no matter when incorporated, can amend their memoranda so as to alter, omit or insert any provisions with respect to their objects or powers as stated in s.172(1) of the Law.

Most companies incorporated after 1 January 1984 in Australia have dispensed with an objects clause and rely on the powers contained in s.161(1) of the Law.

Under s.161(1) of the Law, a company has the legal capacity of a natural person. This means that a company is able to engage in any business or activity and may acquire and exercise rights in the same way as a human being.

However, there are still a large number of companies with an objects clause. These include companies incorporated before 1984 and companies which may wish to restrict their activities to specified objects. They include joint venture companies which are incorporated to carry out a specific project. Under the joint venture agreement, the parties may wish to limit the company's activities to the joint venture purposes.

Section 161(2) of the Law provides that notwithstanding that such companies have objects in the memoranda, the S.161(1) of the Law powers still apply.

As stated earlier the doctrine of *ultra vires* can only have application to a company whose memorandum contains a statement of its objects or other self-imposed restrictions on the exercise of its powers. Even in such cases, the operation of the ultra vires doctrine in Australia is no longer as significant as it once was. This is due to several developments in the Law:-

1) s.161 in effect gives every company the unlimited legal capacity of a natural person.

2) s.162 ensures that the concluded contracts with outsiders cannot be overturned merely because an arrangement breaches a company's objects or other self-imposed restrictions.

3) s.160 assists in the interpretation of ss.161 and 162. It states that their purpose is to abolish the doctrine of *ultra vires* as it applies to dealings with outsiders while at the same time to ensure that a company's objects and powers are given effect to by its officers and members;

4) s.165(1) has abolished the doctrine of constructive notice;

5) the courts have generally broadly construed the objects, particularly the dependent objects; and

6) s.172 gives every company the ability to alter its objects clause.

2.6.1 Section 162 of the Law

The Law however, does recognise that in certain circumstances, ultra vires may be asserted. These circumstances involve matters of an internal nature and is explained in s.160 (b) of the Law. The second object of the Law with respect to the legal capacity of companies is to ensure that the rules of a company relating to objects or powers are given effect to by the company's officers and members, without unduly affecting outsiders in their dealing with the company.

A company contravenes s.162(2) of the Law where :

i) it exercises a power contrary to an express restriction or prohibition contained in its memorandum or articles of association; or

ii) the memorandum contains objects and the company does an act otherwise than in pursuance of those objects.

An officer of a company contravenes s.162 (3) of the Law if the officer is involved in the company's contravention of s.162 (2) of the Law.

However, s.162 (4) of the Law states that neither a company that contravenes s.162 (2) of the Law or an officer who contravenes s.162 (3) of the Law is guilty of an offence.

The policy expressed in s. 160(a) of the Law is given effect by s.162 (5) of the Law. The exercise of a power contrary to a restriction or prohibition contained in the company's constitution or an act outside its objects clause of the memorandum is not invalid merely because of the contravention of s.162 (2) of the Law. Similarly, s.162 (6) of the Law

states that an act of an officer who contravenes s.162 (3) is not invalid merely because the officer contravenes the section.

Despite the effect of s.162 (5) and s.162 (6) of the Law the fact of non- compliance with the objects or any restrictions or prohibitions may still be raised in certain circumstances. These are listed in s.162 (7) of the Law. The fact of non-compliance may be asserted or relied upon only in the following proceedings:

1. A prosecution of a person for an offence against the Law under s.162(7)(c) of the Law. Whilst s.162(4) of the Law makes it clear that an officer who is involved in a contravention of s.162(2) of the Law is not guilty of an offence under the section, under s.162(7)(c) of the Law that contravention may be raised in other contexts. For example, an officer who allows the company to contravene s.162 of the Law may breach either the duty to act honestly or the duty to exercise a reasonable degree of care and diligence under s.232(2) and (4) of the Law and so be guilty of criminal offences under s.1317FA of the Law.

2. An application for an order unders.230 of the Law brought under S.162 (7)(d) of the Law. Section 162(7)(d) of the Law allows the contravention of s.162 of the Law to be raised in the context of an application for an order under s.230 of the Law. This section enables the Australian Securities Commission and certain other persons including a liquidator, members or creditors to apply to the court for an order prohibiting a person from being a director or from taking part in the management of a corporation where the corporation has repeatedly breached the Law and that person

has failed to take reasonable steps to prevent the repeated breaches or where the person repeatedly breached the Law or his or her duties.

3. An application for an order under s.260 of the Law under s.162 (7)(e) of the Law. Section 260 of the Law permits members to seek a remedy where the affairs of a company are conducted in a manner that are oppressive or unfairly prejudicial to or unfairly discriminatory against members or contrary to the interests of the members as a whole. The reference to s.260 of the Law in s.162(7) (e) of the Law indicates that the fact that a company exercises a power contrary to an express restriction or prohibition in its memorandum or outside its objects may involve oppressive or unfair conduct.

4. An application for an injunction under s1324 of the Law to restrain the company from entering into an agreement under s.162 (7)(f) of the Law. Of the six proceedings specified in s.162 (7) of the Law, para (f) can have the most impact on a company's dealings with outsiders. It allows ultra vires to raised in the context of an application for an injunction under s.1324 of the Law to restrain the company from entering into a contract or agreement which is outside its objects or is in breach of a restriction or prohibition contained in the memorandum or articles of association. Section 1324 of the Law allows either the Australian Securities Commission or a person whose interests are effected by conduct that involves a contravention of the Law to apply for an injunction restraining such conduct or possibly requiring that an act or thing be done.

5. Proceedings (other than an application for an injunction) by the company, or a member against the present or former officers under s.162 (7)(g) of the Law. This section allows the contravention of s.162 of the Law to be raised in proceedings by the company, or by a member against the present or former officers. The section appears to include claims for damages against officers for harm caused to a company as a consequence of it entering into an agreement which contravenes s.162 of the Law. This is a statutory exception to the rule in *Foss v. Harbottle* [55] This rule prevents shareholders from enforcing rights against officers whose duties are only owed to the company.

6. An application by the Australian Securities Commission or a member for the winding-up of the company under s.162 (7)(h) of the Law.

2.6.2 Abolition of the Doctrine of Constructive Notice

In their application of the ultra vires doctrine the courts relied on a principle that persons dealing with a company had constructive notice of its memorandum and articles of association. The company could then assert that a contract outside the objects was ultra vires and he could not be bound by the contract. The legislation has recognised the harshness of this and abolished the doctrine of constructive notice. Under s.165 (1) of the Law, a person is not taken to have knowledge of the memorandum or articles of association or any other public document or particulars by reason only that they have been lodged with the Australian Securities Commission. This means that an unexecuted,

[55] (1843) 2 Hare 461; 67 ER 189

but binding agreement with an outsider cannot be restrained under s.162 (7)(f) of the Law on the basis that it was ultra vires and that the outsider had constructive notice of the company's objects. In addition, persons dealing with a company are entitled to make certain assumptions under s.164 (3) of the Law. These include an assumption that the memorandum and articles of association have been complied with, as stated in s.164 (3)(a) of the Law. The abolition of the doctrine of constructive notice has improved the position of outsiders dealing with a company. It is now more difficult for companies to avoid their contractual obligations.

2.7 Conclusion

The ultra vires doctrine was once a serious trap for those contracting with a company. Ingenous drafting of the objects clause and legislative intervention has drawn the sting of the doctrine.

England, the original source of our Company Law has gone to almost the extent of granting full capacity to companies. Australia has taken a bolder step and has given full legal capacity to companies. Both the English and Australian legislatures have recognised that some parts of the old doctrine are beneficial and must remain and therefore have preserved it statutory provisions. In England, directors are under a duty to the company and its members to adhere to a company's objects clause. Again in England, a member could restrain a proposed ultra vires transaction provided that no legal obligation has arisen between the company and a third party. Australia has provisions in its Corporations Law which achieve similar results where the company chooses to state its

objects clause in its memorandum of association. Both legislatures have abolished its constructive notice doctrine.

Malaysia has continued to pin its faith in its s.20 (1) of the Companies Act 1965. Section 20(1) abolishes the application of the doctrine between a company and a third party. An unusual feature of the Malaysian provision is that a member or a holder of a debenture secured by a floating charge can restrain performance of an ultra vires act even though a binding agreement has arisen between the company and a third party, as long as the transaction remains executory and remains to be performed. Although the third party may receive compensation by virtue of s.20(3), the compensation is limited. A pertinent point to note about the Malaysian statutory provisions on ultra vires is the absence of a clear and express provision abolishing the Common law doctrine of constructive notice. Thus technically it is possible for a court to nullify the effect of s.20 (1) by ruling that the Common law doctrine still applies in Malaysia. The application of the Common law doctrine will make s.20 (1) a dead letter. Such a ruling is extremely remote bearing in mind the legislative intent behind s.20 (1). However, a clear statutory provision clarifying the position would be useful.[56]

[56] See the views expressed by Balan & Talat Mahmood , "Doktrin Ultra Vires dan Seksyen 20 Akta Syarikat 1965", an article to be published in the Journal of Malaysian & Comparative Law (JMCL) Vol.23.

CHAPTER 3

THE AGENTS OF THE COMPANY

3.1 Introduction

As stated earlier, a company is an abstract entity, and it can only enter into contracts through the actions of a natural person. Section 35 (4) of the Companies Act 1965 (hereinafter referred to as the 'Act')[1]. provides that so far as concerns the formality of making a contract, a person acting under the express or implied authority of a company, may make a contract in the name of or on behalf of the company in the same manner as if that contract were made by a natural person.

This indicates that a company may enter into a contract directly through one of its organs, usually the board of directors, or through a person who represents the mind and will of the company. This type of situation is governed under the organic theory of company law which largely lies outside the law of agency but draws upon it.

A company may also enter into a contract indirectly through an agent. The agent may be an officer or employee of the company. Whether a company will be liable under a contract for the acts of an officer or agent is governed under the general law of agency. These agency principles have been modified by the common law and the Act so as to recognise the abstract nature of companies. The agency rules which are applicable to

[1] Act 125

companies are subject to the common law rules as to the doctrine of constructive notice and a special set of principles known as the "rule in *Turquand's case*" and its exceptions.

Whenever there is a delegation of power to an agent, that agent is given some sort of authority by the principal. This authority is the actual authority of the agent. This authority may be express or implied authority. Express authority is that which is expressly conferred upon the agent. Implied authority is not expressly stated; it is authority implied by the circumstances. This may be of two forms: authority to do things incidental to matters that the agent is expressly authorised to do so,[2] and authority to do things that a person in that position usually does[3] . This type of implied authority is sometimes known as "customary" or "usual" authority.

3.2 ACTUAL AUTHORITY

Actual authority arises where the principal has given consent to the agent to act for the principal [4] . This may derive from an express or implied conferral of authority by the principal to do certain acts or enter into a particular transaction.

Section 139 of the Contracts Act 1950[5] states that the authority of an agent may be expressed or implied. Further s. 140 of the Contracts Act 1950 defines what is an express and implied authority. It states that an express authority is when authority is given by words spoken or written and an implied authority is said to be inferred from the

---

[2] *Pole v. Leask* (1860) 28 Beav 562, 575 per Sir John Romilly MR (Master of the Rolls' Court, England); affirmed by the House of Lords. (1863) 33 LJ Ch 155

[3] *Hely - Hutchinson v. Brayhead Ltd.* [1968] 1 QB 549, 583 per Lord Denning MR (Court of Appeal, England).

[4] Ford and Austin's Principles of Corporations Law 7th ed. Butterworths 1995 p. 505

[5] Act 136

circumstances of the case; and things spoken or written , or the ordinary course of dealing, may be accounted circumstances of the case.

The extent of the agents authority is given in s.141(1) and (2) of the Contracts Act 1950. It states that if an agent has authority to do an act, he has the authority to do every lawful thing which is necessary in order to do the act or if the agent has authority to carry on a business, he has authority to do every lawful thing necessary for the purpose, or usually done in the course of conducting such business.

In a company context, an agent may be conferred actual authority by some statute. For instance, section 57(4) of the Criminal Procedure Code[6] provides that the managing director of a company is authorised to appoint a person to represent the company if it is charged with an offence. Authority may also be conferred upon a particular agent by the memorandum or articles of association. More commonly, however, the board of directors may appoint agents and delegate duties and functions to them[7]. An agent may also be conferred authority to act by the general meeting acting within its sphere. Finally, the company's agents may be authorised to delegate authority to sub-agents.

Further, an officer or agent will often have implied authority. A company will usually give consent to an agent to act for it by appointing the agent to a particular position.

Generally, the articles will confer a wide power of management on the board of directors[8]. In the usual case, the board is the organ of the company for the purposes of management so that its acts are the acts of the company itself. The authority of the board

---

[6] Cap 68

[7] Art.91 of Table A envisages that the board of directors may delegate any of their powers to a managing director.

[8] See Table A art 73

in this respect, stems directly from the articles. While the board is more than an agent as regards contracts between a company and an outsider it has actual authority in the same way as an agent may have actual authority to act for the company.

However, outsiders do not deal directly with the board. Rather, they deal with a person to whom the board has delegated some or all of its functions. This person may be appointed as managing director of the company[9] upon whom the directors may confer any of the powers exercisable by them[10] .

The appointment of a person as managing director results in that person having the implied authority usually associated with that position. The implication arises from the facts of the appointment as managing director and the usual or customary authority of a managing director in the circumstances of the company and the nature of its business.

In certain cases, the appointment of a person to a position other than managing director may also create agency by implied authority. In *Brick and Pipe Industries Ltd v Occidental Life Nominees Pty Ltd*[11] , a director was taken to have implied authority to act as the company in circumstances where he had the controlling shares and assumed the role of managing director with the acquiescence of the other directors. Transactions had generally been entered into without prior reference to the board and no attempt was made to interfere with this assertion of the control.

The acquiescence of members of the board to the conferral of actual authority requires,

---

[9] See Table A art 76(1)

[10] See Table art 91(1)

[11] (1992) 10 ACLC 253

"not merely the silent acquiescence of the individual members of the board, but the communications by words or conduct of their respective consents to one another and to the agent" [12]

Normally, the appointment of a person as a director does not carry with it the implied authority to bind the company.[13] The powers of management under the articles is conferred on the board as a collegiate body. In the case of *Dart Sum Timber (Pte) Ltd v Bank of Canton Ltd* [14] it was held that an individual director has no authority as such to make contracts on behalf of his company, even if he is chairman of the board of directors unless he is expressly authorised to do so.

Lord Justice Browne - Wilkinson in the case of *Rolled Steel Products (Holdings) Ltd v British Steel Corporation & Ors.*[15] said

" Apart from questions of ostensible authority, directors like any other agents can only bind the company by acts done in accordance with the formal requirements of their agency.... Acts done otherwise than in accordance with these formal requirements will not be the acts of the company."[16] .

Hence, where powers are not exercised in the manner prescribed by the articles or the Act, the power when exercised cannot be legally classified as an act of the company unless the principle of unanimous consent is applicable.

---

[12] per Diplock J in *Freeman and Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480

[13] *Northside Developments Pty Ltd v Registrar -General* (1990) 8 ACLC 611 at p 645 per Dawson J.

[14] (1982) 2 MLJ 101 (Court of Appeal, Singapore)

[15] [1985] 3 All ER 52

[16] Ibid at p. 91-92

In *Kelapa Sawit (Teluk Anson) Sdn. Bhd. v Dr Yeoh Kim Leng & Ors*[17] the articles of association of the company, in particular article 54, empowered the directors to pass circular resolutions and the circular resolutions signed by all directors would be as valid and effected as if it had been passed at a meeting of the directors duly constituted. It also provided that the seal of the company may only be affixed under the authority of a director's resolution and in the presence of a director and a secretary both of whom were also required to sign every document to which the seal of the company was affixed. Following the practice of the plaintiff to issue shares to its members as capitalisation of loans or debts which may be owed to the members, a circular resolution was purportedly passed to allot shares. The circular resolution, was however, only signed by three and not by all the directors. Additionally, the share certificates were already signed and sealed when the circular resolution was presented to the three directors for their respective signatures.

The Supreme Court (now the Federal Court) held that the general rule is that directors may only exercise their powers collectively by passing resolutions at board meetings unless the articles otherwise provide. While the directors were empowered to pass the circular resolution, they would only have done so in the manner prescribed by the articles and likewise, the directors could not have signed and sealed the share certificates in the absence of the prior resolution. In view of these irregularities, the allotment of the share would not be described as an act of the company and hence was a nullity.

---

[17] (1991) 1 MLJ 301

The appointment of a person as secretary of a company confers implied authority to make contracts in connection with the internal administration of the company but not in relation to the management of the company in the sense of carrying on the company's business[18] .

Whether a chairman of directors has implied authority to bind a company is not entirely clear. The usual functions of a chairman do not generally extend to conducting the company's business operations [19] and a chairman has no more authority to bind the company than has any other single director.[20] Ford suggests that as a chairman commonly receives more remuneration than other directors, there may be some things that the chairman of a public company is impliedly authorised to do which is beyond the usual authority of a single director.[21]

While the usual authority of a chairman is unclear, the existence of implied authority may be determined from the circumstances and conduct of the company and its chairman in the same way as occurred in the *Brick and Pipe* case. This arose in *Equiticorp Finance Ltd v Bank of New Zealand*[22] . The Equiticorp Group comprised of companies in its finance arm and other companies in an industrial arm. Hawkins was chairman of the Group and director of a number of companies. A company in the industrial group borrowed money from a bank. The bank required early repayment and Hawkins applied

---

[18] *Panorama Developments (Guilford) Ltd v Fidelis Furnishings Fabrics Ltd* [1971] 2 QB 711 and *Northside Developments* at 645 per Dawson J.

[19] *Hughes v NM Superannuation Pty Ltd* (1993) 11 ACLC 923

[20] *Hely-Hutchinson v Brayhead Ltd* [1968] 1 QB 549

[21] Note 524 at p 105 , Ford 's Principles of Corporations Law (6th Ed.)

[22] (1993) 11 ACLC 952

assets of two member companies of the finance arm with the tacit approval of all but one of the directors of the finance arm companies. There was no formal approval for the transfer of assets from the board of the finance arm companies. When the companies went into liquidation, they sought recovery of the assets on the ground, among others, that the payment of the assets was unauthorised by the two companies.

Clarke and Cripps JJA, in a majority judgment, held that the business of the various companies in the Equiticorp Group was conducted under the general authority of Hawkins who undertook all decisions of significance either with or without consultation with senior members of management. In these circumstances, Hawkins had implied authority to apply the assets of the finance companies in the manner in which he directed.

In a dissenting judgment, Kirby P held that no implied authority had been conferred on Hawkins. He stated :

> "Where, however, actual authority is held to be implied, it remains vital to ask the question: 'authority for what?' It cannot be an authority at large to do anything at all. Relevantly, it must be authority to do something apparently in the best interests of the company.[23]

Kirby P also found that the other directors were either unaware of the disposal of the assets or were opposed to it. This did not amount to acquiescence at the time in the transfer of the assets. In his judgement, Kirby P noted that outsiders should be protected in their dealings with companies which operate in an irregular way and are dominated and effectively controlled by particular individuals. Kirby P said,

---

[23] (1993) 11 ACLC 952 at p 978

"it is to debase the integrity of company law, and the obligations of companies to operate according to law, to extend the protective principle to cloak Mr Hawkins with implied actual authority .... The suggested imperative of "realism" and the real politic of corporate control does not authorise courts to ride roughshod over the due observance of company law."[24]

This dissenting judgment emphasises the balance of interests which is at the heart of determining when a company is to be bound by the unauthorised acts of its officers. These considerations form the basis of the common law principles.

3.3 APPARENT AUTHORITY

An agent's apparent or ostensible authority creates the agency relationship because of the appearance of authority conferred on the agent. It does not depend on any agreement or relationship between principal and agent. It is often the case that an outsider does not know whether an agent has actual authority and the extent of that authority. Usually, all the outsider relies on is the appearance of authority. Depending on the circumstances, the extent of an agent's apparent authority may be the same as the agent's actual authority or it may exceed the scope of the agent's actual authority.

In some situations a person may have apparent authority to do particular acts for the principal even though that person has been given no actual authority to contract. Thus actual and apparent authority rest upon entirely different basis but may often overlap.

If an agent's apparent authority can be established, it creates an agency by estoppel. This means that as between principal and outsider, the principal is prevented or estopped from

[24] Ibid at p. 978

denying that the agent lacked authority. An agency by estoppel creates a contract between the principal and outsider in the same way as a contract is created by an agent with actual authority.

The representation of the agent's authority must be made by the principal to the outsider. A principal is not liable merely on the representations of the agent. Where an outsider deals with a particular person, it may be difficult to determine whether the dealing is with the company or only with that person. In particular, is a representation made by a person acting as an officer to be taken as representations by the company?

The principal may expressly make the representation to the outsider. It is more usual for the representation to arise by the principal's conduct. A representation by conduct may take either one of two forms:

i) it may arise when the principal permits the agent to occupy a particular position. In such cases the principal represents or holds out that the agent has the customary authority of a person in such a position. In this respect it is similar to an agent with implied actual authority resulting from the position occupied.

ii) it may also arise when the principal's conduct permits the agent to carry out particular tasks on the principal's behalf which are beyond the scope of the agent's customary authority. For example, a single director may be permitted by the company to contract on its behalf in a number of previous transactions. This is a holding out that the director's authority is greater than would normally be the case. Apparent authority typically arises where a person is allowed by the board to act as a managing director even though not appointed to this position. Apparent authority may arise even though implied actual

authority may not have been conferred because the board had not acquiesced to the particular person assuming the role of managing director.

In *Freeman and Lockyer v Buckhurst Park Properties (Mangal) Ltd* [25] there were two controllers of a company formed for the purpose of developing a property. Each held half of the issued shares and they comprised the board together with a nominee of each. The quorum of the board was four. One of the two controllers was absent for a long period. The other controller acted as managing director with the approval of the board, even though he had not actually been appointed. The articles were of similar effect to Table A art. 76 and conferred a power on the board to appoint a managing director. The de facto managing director entered into contracts related to the property development business of the company. One of these contracts was with a firm of architects which sought to enforce the contract after the company refused to pay its fees. The Court of Appeal held that the company was bound by the acts of its de facto managing director. It had represented through its board that its agent was the managing director if the company. The contract was within the customary authority of a managing director and the outsider had relied on this apparent authority.

Diplock LJ stated four conditions which must be met in order for a company to be bound by the acts of an agent where the agent had no actual authority to so act :

a) a representation must be made to the outsider that the agent had authority to enter into the kind of contract the outsider seeks to enforce;

[25] [1964] 2 QB 480

b) the representation must be made by someone with actual authority to manage the company's business or at least authority in respect of the matters relating to the contract;

c) the outsider must be induced by the representation to enter into the contract and in fact relied upon the representation;

d) the memorandum or articles do not deprive the company of the capacity to either enter into the type of contract concerned or to delegate authority to enter into that kind of contract to the agent.

The last of these conditions refers to acts which are ultra vires the company in the sense of being outside the objects clause in the memorandum. Ultra vires contracts have been dealt with in Chapter 2. The last condition also requires the articles to authorise a delegation of authority to enter into the type of contract concerned. This power to delegate is usually conferred by articles in a form similar to Table A art 76 of the Articles of Association.

The condition which has caused the most uncertainty from the outsider's point of view has been the second. This requires the representation to be made by someone with actual authority to manage the company's business or in respect of matters to which the contract relates. In the *Freeman and Lockyer* case, this did not present a problem to the outsider because the representation or holding out was made by the board through its acquiescence to the de facto managing director acting as such. Usually, an outsider will be in contact with someone to whom the board has delegated authority. It will be difficult for the outsider to determine the nature and extent of this authority. This

becomes critical where the board has represented that someone has apparent authority to bind the company and this person then purports to cloak another person with apparent authority. Such a situation does not meet the second of Diplock LJ's conditions. This fact situation arose in the Australian High Court case of *Crabtree-Vickers Pty Ltd v Australian Direct Mail Advertising Co Pty Ltd* [26] in which the court approved of the principles stated by Diplock J in *Freeman and Lockyer*. A de facto managing director was found to lack actual authority because he had not been formally appointed. An employee of the company was a member of a board committee to whom the board had delegated the power of management. This employee has been held out by the de facto managing director to have the necessary authority to enter into a contract on behalf of the company. The High Court applied the principles formulated by Diplock LJ and held that the employee had no actual authority. He also did not have apparent authority because the representation was made by someone who himself only had apparent authority to carry on management of the company. The de facto managing director had apparent authority on the same basis as was the case in *Freeman and Lockyer*. This person did not have actual authority because he had not been formally appointed. In order for the representation in this case to have been made by someone with actual authority, it would need to have been made by either the board or the committee of directors. It seems curious that a de facto managing director may bind the company through his apparent authority based on a representation by the company and yet, such a person is unable to represent that someone else has apparent authority. If a company can be bound by a

---

[26] (1976) 50 ALJR 203

contract, in circumstances such as that which arose in *Freeman and Lockyer*, it is hard to see why the company cannot be bound by a representation of the same person which holds out that someone else has authority to bind the company. This problematic result could be avoided if the de facto managing director is regarded as having implied actual authority because the board acquiesced to his assumption of broad powers.

This strict adherence to the conditions enunciated in the *Freeman and Lockyer* case produces considerable difficulties and uncertainty to an outsider. The outsider is required to ascertain the validity of a conferral of authority on the managing director in circumstances where the dealings are not with the board or a committee to whom authority has been delegated.

To the outsider, the circumstances indicate a holding out by the company because it appears to have allowed the representation to be made. The application of agency law requires the representation to be made by an organ of the company, such as its board or a person or persons to whom authority has been delegated, such as managing director or committee of directors. In the latter case, the outsider must hope that the authority was properly conferred on the committee so as to constitute actual authority. This places outsiders dealing with any person who does not possess actual authority in a potentially perilous position and yet it may be difficult or impossible for an outsider to ascertain the nature of the authority.

3.4 CUSTOMARY AUTHORITY

Where an officer or agent of the company exercises authority which is not customary for someone in that position to normally have, the agent does not have implied authority or

apparent authority to bind the company. The customary authority of particular officers is relevant in considering the limits of both implied actual authority and apparent authority.

3.4.1. Customary Powers and Duties of Directors

While it is usual for the board as a whole or a managing director to be conferred with very wide powers of management, it is not usual for an individual, ordinary director to have such authority. In *Northside Developments Pty Ltd v Registrar General*[27] , Dawson J considered the authority of an individual director.

> "The position of director does not carry with it an ostensible authority to act on behalf of the company. Directors can act only collectively as a board and the function of an individual director is to participate in decisions of the board. In the absence of some representation made by the company, a director has no ostensible authority to bind it".

In the case of *Dart Sum Timber (Pte.) Ltd. v. Bank of Canton Ltd.*[28] the court held that an individual director has no authority to make contracts on behalf of his company, even if he is the chairman of the board of directors , unless he is authorized to do so.

It should be noted that while the customary authority of directors is limited, they may still be able to bind the company, if they have actual authority, or there has been a representation or holding out by the company that they have greater authority than is customary for directors.

---

[27] (1990) 8 ACLC 611 at p 645

The articles of association frequently give individual directors the power to:

a. authenticate the company's common seal: Table A, art.96;

b. sign the company's negotiable instruments, including cheques and receipts on behalf of the company: Table A, art.77.

In *Brick and Pipe Industries Ltd. v. Occidental Life Nominees Pty.Ltd.*[29], a dominant director was taken to represent the mind and will of the company and have the authority of a managing director where the other directors acquiesced to this and did not involve themselves in transactions entered into by the dominant director. In the absence of the acquiescence of other directors, and individual director does not have customary authority to represent that someone else had been appointed as secretary. This can be enunciated from the New Zealand case of *Bank of New Zealand v. Fiberi Pty.Ltd.*[30].

3.4.2. Customary Powers and Duties of Secretaries

A company secretary may in certain circumstances act as an agent of the company. The implied authority or apparent authority of a company secretary extends to making contracts on behalf of a company which relate to the administration or internal workings of the company. In this respect, the customary authority of the company secretary has expanded substantially over the past century.

---

[28] [1982] 2 MLJ 101 (Court of Appeal , Singapore).

[29] Supra note 11

[30] (1994) 12 ACLC 48.

The early cases held that a secretary had no customary authority to bind a company. In *Newlands v. National Employers' Accident Assoc.,*[31] Brett MR said:

> "A secretary is a mere servant; his position is that he is to do what he is told, and no persons can assume that he has any authority to represent anything at all."

A similar restrictive view was taken in *Ruben v. Great Fingall Consolidated*[32]. In that case, the secretary issued false share certificates by forging the signatures of the company's directors. He then used the share certificates as security for a loan to himself. The lender sued the company on the basis of the untrue information contained in the share certificate.

The House of Lords held that company was not liable because the forgery rendered the certificate a "pure nullity". The secretary had no actual or apparent authority to warrant the certificate was genuine.

Lord MacNaughten said:

> " The secretary of the company, who is a mere servant, may be the proper hand to deliver out certificates which the company issues in due course, but he can have no authority to guarantee the genuineness or the validity of a document which is not the deed of the company."

---

[31] (1885) 54 LJ (QBD) 428

[32] [1906] AC 439

As stated earlier, Lord Denning MR considered this question in *Panorama Developments (Gilford) Ltd v Fidelis Furnishing Fabrics Ltd*[33] A company secretary entered into a contract for the hire of cars for the purpose of carrying the company's major customers. The secretary then used the cars for his own purposes. The car hirer sued the company on the basis that its secretary had apparent authority to enter into that contract. Lord Denning stated:

> " A company secretary is a much more important person nowadays than he was in 1887. He is an officer of the company with extensive duties and responsibilities.... He regularly makes representations on behalf of the company and enters into contracts on its behalf which come within the day-to-day running of the company's business. So much so that he may be regarded as held out as having authority to do such things on behalf of the company. He is certainly entitled to sign contracts connected with the administrative side of a company's affairs, such as employing staff, and ordering cars and so forth. All such matters now come within the ostensible authority of a company's secretary."[34]

The role of the secretary clearly does not extend as far as that of the directors. It is limited to matters of an internal nature. Dawson J in the *Northside* case held that the office of secretary did not carry with it any apparent authority to affix the company seal and mortgage a company's land nor to enter into,

---

[33] (1971] 2 QB 711 at pp 716-7. The distinction between managerial and administrative acts was also referred to in *Club Flotilla (Pacific Palms) Ltd. v. Isherwood* (1987) 12 ACLR 387 and *Mohamed bin Othman & Anor. v. Abdul Shattar bin Abdul Rahman & Ors.* [1987] 2 MLJ 695.

[34] Per Lord Denning in *Panorama Development (Gilford) Ltd. v. Fidelis Furnishing Fabrics* (1971) 2Q.B. 711 at p. 716- 717

"commercial transactions upon his own decision which are not of an administrative kind required for the daily running of the company's affairs".[35]

Where an outsider deals with a secretary or individual director who is acting outside the usual authority of an officer of the type concerned, the outsider loses the protection which arises from reliance on apparent authority. From the outsider's point of view this presents difficulties because it is rare for the outsider to deal directly with the board. Usually, the outsider deals with someone whom it may reasonably be assumed has been delegated to act on behalf of the board. It may be difficult for the outsider to determine whether the officer or agent is acting with actual or apparent authority and the extent of the authority conferred by the board.

An outsider dealing with a company will usually be in a stronger position if dealings were conducted with a managing director. The articles will usually empower the board to appoint a managing director to exercise such of the board's powers at it thinks fit[36] .

3.4.3. Customary Powers and Duties of Managing Directors

A managing director is invested with the customary authority to carry on the company business in the usual way and do all acts and enter into all contracts necessary for that purpose. Thus, he may sign cheques on the company's behalf[37] , even in favour of himself[38] , borrow money on the company's account and give security over the company's property for its repayment[39] , receive payment of debts owed to the

---

[35] (1990) 8 ACLC 611 at p 645

[36] Table A art 76 is a typical example.

[37] *Dey v. Pillinger Engineering Co.* (1921) I K B 77

[38] *Bank of New South Wales v Goulburn Valley Butter Co. Pty Ltd* (1902) AC 54

[39] *Biggerstaff v Rowatt's Wharf Limited* (1896) 2 Ch. 93

company[40] , guarantee loans made to the company 's subsidiary, agree to indemnify persons who have given such guarantees themselves [41] and to initiate legal proceedings on behalf of the company[42] .

The customary authority of the managing director is however confined to commercial matters and so he has no customary authority to approve transfer of shares in the company or to alter its register of members[43]. The limits of the customary authority of the managing director are however not entirely clear.

Therefore, where an officer or agent of a company acts outside the customary authority of a person occupying the particular position concerned, the company may still be liable if it has held out that its officer or agent possesses greater authority than would be usual. This holding out must have been made by someone who has actual authority to make such a representation to the company. Where such a representation has been made, the outsider may still enforce the contract even though the agent of the company was not validly appointed or the agent acted outside the customary authority of a person occupying the particular position concerned.

3. 5 Conclusion

The actual authority of an agent is a relationship between the principal and the agent; the rest of the world is a stranger to this relationship. The third party dealing with the agent of a company does not know what the agent's actual authority is, nor in most cases can he

---

[40] *Clay Hill Brick & Tile Co Ltd v Rawlings* (1938) 4 ALL ER 98

[41] *British Thomson - Houston Co Ltd v Federated European Bank Ltd* (1932) 2 KB 176

[42] *Avel Consultants Sdn Bhd v Mohd. Zain Yusof* suit no. 336 of 1984 (unreported)

[43] *George Whitechurch Ltd v Cavanagh* (1902) AC 117

find out. Sometimes the authority of agent to do certain acts depends on compliance with certain formalities or there is some irregularity in the management which vitiates the authority conferred upon the agent. A party outside the company has no way of determining whether the company's internal regulations have been complied with. However, the law does not require an outside party to do so. If an agent has an apparent authority to do an act, a person dealing with the company is entitled to assume that all matters of internal management and procedure prescribed by the articles of association have been complied with. This is known as the "rule in *Turquand's* case" or the "indoor management rule" and this will be dealt with in the following chapter.

CHAPTER 4

THE RULE IN TURQUAND'S CASE

4.1 Introduction

Person's dealing with a company and contracting in good faith may assume that "acts within its constitution and powers have been properly and duly performed and are not bound to inquire whether acts of internal management have been regular." [1]

The application of this rule gives rise to a presumption which prevents the company from avoiding a contract by relying on the fact that the proceedings were irregular and the person acting for the company was unauthorised to do so. This serves to protect persons "who are entitled to presume, just because they cannot know, that the person with whom they deal has the authority which he claims"[2] .

At common law, the doctrine of constructive notice operated against outsiders dealing with companies. However, this doctrine did not operate where the directors or other agents of a company acted outside their authority but this was not apparent from the articles or other public documents of the company. The

[1] Halsbury's Laws of England 4th ed 1988 Vol 7 (1) par 980. This statement was approved by Lord Simonds in *Morris v Kanssen* [1946] AC 459 at p 474.

[2] per Lord Simonds in *Morris v Kanssen* (above)

Rule in *Turquand's*[3] case states that while persons dealing with a company are taken to have constructive notice of the contents of the company's public documents, they need not go further to ensure that the internal proceedings of the company have been properly carried out. In fact, the outsider can assume that these proceedings were properly carried out.

In *Royal British Bank v Turquand*, [4] the deed of settlement, the equivalent of the memorandum and articles of a company, empowered the board of directors to borrow such sums as were authorised by a resolution of the general meeting of the shareholders. The company borrowed money from a bank on the authority of two of its directors who authenticated the company's common seal. There was no authority given by the general meeting. The company refused to repay the loan and argued that the bank had constructive notice of the articles and should have been aware of the lack of authority. It was held that an outsider need not inquire into whether such a resolutions had in fact been passed. The company was bound to the bank because the passing of the resolutions was a matter internal to the company. Jervis CJ said:

> "... the party here, on reading the deed of settlement, would find, not a prohibition from borrowing, but a permission to do so on certain conditions. Finding that the authority might be made complete by a resolution, he would

---

[3] *Royal British Bank v.Turquand (1856) 6 E & B 327; 119 ER 886*

[4] Supra note 3

have a right to infer the fact of a resolution authorising that which on the face of the document appeared to be legitimately done". [5]

The Rule in *Turquand's* case grew naturally as a response to the development of the doctrine of constructive notice. While outsiders had constructive notice of matters they could discover for themselves from public documents such as the articles, they could not reasonably be taken to have notice of matters concerning the indoor management of the company.

In the case of *Mahoney v. East Holyford Mining Co.*[6] Lord Hatherly said:

> "When there are persons conducting the affairs of the company in a manner which appears to be perfectly consonant with the articles of association, those so dealing with them externally are not to be affected by any irregularities which may take place in the internal management of the company."[7]

When an outsider is dealing with the board or those authorised by it, the case of *Morris v. Kanssen*[8] states that the Rule applies where there has been a valid appointment which has not been vacated and not where there has been "no appointment."

If an outsider is dealing with officers not so authorised to act on behalf of the company, that the outsider is entitled to rely on the Rule if the person through whom the outsider dealt with occupies a position in the company such that it

---

[5] (1856) E & B 327 at p 332

[6] (1875) L.R. 7 H.L.869

[7] at p. 894

[8] [1946] A.C. 459

would be usual of that position to have authority to bind the company in relation to the transaction concerned unless the outsider knows of the contrary or knows of facts which would put a reasonable person on inquiry.[9] Thus, if the person acting for the company is its chief executive or managing director, then, he may be safely be assumed to be authorised. In practise, he will probably have actual authority[10] but even if he has not he will have ostensible authority and his acts will bind the company.[11] Much of the same applies to other executive directors except that if the descriptions of their posts suggest particular areas of responsibility ("finance director" or "sales director") they cannot be assumed to have authority outside those areas. Even though individual non-executive directors have no responsibility unless the board delegates it to them[12] they may be assumed to have some individual authority, beyond that of sharing in the exercise of the board's collective authority at meetings of the board.[13] Moreover, it is not uncommon for the board of directors to allow one of the director to assume the position of managing director even though he has never been formally appointed to that position and in these circumstances the courts have treated him as if he were the managing director.[14]

When the outsider deals with an officer or employee below the level of director,

---

[9] *Underwood Ltd. v. Bank of Liverpool* [1924] 1 K.B. 715,C.A.

[10] *Hely-Hutchinson v. Brayhead Ltd.* [1968] 1 Q.B. 549, C.A.

[11] *Freeman & Lockyer v. Buckhurst Park Properties Ltd.* [1964] 2 Q.B 480, C.A., especially the judgement of Lord Diplock L.J. at 506.

[12] *Rama Corporation v. Proved Steel & General Investment Ltd.* [1952] 2 Q.B. 147

[13] *Heng Wan v. Selangor Rice Mill Co.* [1967] 2 MLJ 44

[14] *Clay Hill Brick Co. v. Rawlings* [1938] 4 All E.R. 100

the position is more problematical and, until recently the courts have shown a marked reluctance to recognise any ostensible authority even of a manager.[15] However, this is now changing and it may be taken that a manager, even if he does not have actual authority, will have ostensible authority to undertake everyday transactions relating to the branch of business which he is managing[16] and the secretary will similarly have such authority in relation to administrative matters.[17] An officer or agent of the company cannot, however, confer ostensible authority on himself by representing that he has actual authority.[18] It can only be conferred by conduct of the company, acting through an organ or agent of the company, such as the board or the managing director, with actual or apparent authority to make representations as to the extent of the authority of the company's agents. Therefore, if the company has made such representation on which the outsider has acted in good faith, the outsider may rely on the Rule.

It can be seen that protection afforded to an outsider who has dealt with an employee is considerably less than that afforded to one who has dealt with the board of directors or someone actually authorised by the board.

In Australia, the operation of the rule in *Turquand's* case was considered by the High Court in *Northside Developments Pty Ltd v Registrar - General*[19] . The

---

[15] *Kreditbank Cassel v. Schenkers* [1927] 1 K.B. 826

[16] *Armagas Ltd. v. Mundogas S.A.* [1986] A.C. 717, H.L.

[17] *Panorama Developments Ltd. v. Fidelis Furnishing Fabrics Ltd.* [1971] 2 Q.B. 711,C.A.

[18] Supra note 15.

[19] (1990) 8 ACLC 611

common seal of Northside was affixed to a mortgage document which secured a loan from Barclays to a company controlled by Sturgess, a director and shareholder of Northside. The mortgage was over land owned by Northside and was its only major asset. The common seal was affixed and signed by Sturgess as director and by his son who purported to sign as the company secretary. The son had not been appointed under the articles although a statutory return filed with the Commission named him as the company secretary. The other two directors, who were also the remaining shareholders, did not know of or authorise the execution of the mortgage, nor did they know of the purported appointment of secretary. They had no interest in the borrowing company and Northside derived no benefit from the transactions. The High Court considered the validity of the mortgage. This depended upon whether it had been executed by Northside. The case was decided under the common law. The High Court held that Northside was not bound by the mortgage because the affixing of the common seal was invalid. Although the Rule in *Turquand's* case enabled Barclays to assume that the common seal was properly affixed and the internal proceedings of the company had been properly carried out in accordance with its memorandum and articles, the circumstances of the case should have put Barclays upon inquiry. Since Barclays failed to make further inquiries as to whether the common seal was properly affixed it was unable to rely on the *Rule in Turquand's* case and Northside was not bound by the mortgage.

The circumstances which put Barclays upon inquiry were that the mortgage secured Northside's major asset where the transactions were outside its usual business and not for its benefit. Barclays was prevented from relying on the Rule in *Turquand's* case because it ought to have suspected an irregularity. Barclays did not have to have actual knowledge of the lack of authority of Sturgess and his son to affix the company seal.

Mason CJ stated the policy behind the Rule in *Turquand's* case.

> "What is important is that the principle and the criterion which the Rule in Turquand's case presents for application give sufficient protection to innocent lenders and other persons dealing with companies, thereby promoting business convenience and leading to just outcomes. The precise formulation and application of that rule calls for a fine balance between competing interests. On the other hand, the rule has been developed to protect and promote business convenience which would be at hazard if persons dealing with companies were under the necessity of investigating their internal proceedings in order to satisfy themselves about the actual authority of officers and the validity of instruments."[20] .

The Rule in *Turquand's* case protects an outsider where there is an irregularity concerning the proper holding of a meeting. For example, a quorum may not have been present, inadequate notice may have been given or a voting irregularity may have occurred. The obscurity surrounding the Rule in *Turquand's* case has

[20] (1990) 8 ACLC 611 at pp 627-2 per Mason CJ.

resulted in significant differences of opinion in attempts to express the basis of the Rule and its inter-relationship with agency principles.

Campbell suggests that the principle of estoppel is not an adequate explanation of the Rule[21]. While a company may make a representation by means of its articles, if the articles state that the authority of an agent is subject to a condition, this does not constitute a representation that the condition has been fulfilled. Therefore, if the articles empower the board to delegate some or all of its functions, the company does not thereby represent that a delegation was in fact made.

Campbell is of the view that the Rule in *Turquand's* case goes far beyond the principle of estoppel as its effect is to hold a company bound by a contract even in the absence of actual or apparent authority. Campbell does not cite any example of where a company was bound by a contract where an agent lacked actual and apparent authority.

Although the High Court judges in the *Northside case* adopted different approaches, they all suggested that in agency situations, the Rule did not apply in the absence of authority.

Ford and Austin[22] suggest another theoretical basis behind the Rule in *Turquand's* case which they consider to be the best supported by weight of authority. This is referred to as the "closed door rationale" for the Rule which is designed to allow outsiders to make protective assumptions just because they

---

[21] Thompson "Company Law - Doctrines and Authority to Contract" (1956) 11 Univ. of Toronto LJ 248 at p 254.

[22] Ford HAJ and Austin RP- Ford's Principles of Corporations Law 7th ed Butterworths p 524

cannot know that the person with whom they deal has the authority which he claims.[23]

In the context of a transaction entered into by a company and a bank, Kirby P of the New South Wales Court of Appeal in *Registrar-General v Northside Developments Pty Ltd*[24] expressed reservations on the justification of the Rule. Outsiders such as banks are generally in a very strong commercial position to insist on detailed scrutiny of the internal workings of a company.

4.2 The Rule in Turquand's Case and Agency Principles

The general principles of agency law in their application to companies operate in conjunction with the Rule in *Turquand's* case.

We have seen that the operation of the rule enables an outsider to presume that the indoor management of a company has been carried out in a regular manner. This enables an outsider to show that a company has given either actual or apparent authority to an officer or agent of the company. It also enables an outsider to presume that where a company enters into a contract directly by itself, the person who acted for the company were properly authorised to do so. This is particularly relevant where the common seal of the company was affixed by persons purporting to act as directors or secretary with authority to affix the company seal.

---

[23] per Lord See *Morris v Kanssen* [1946] AC 459 Simonds at p 475

[24] (1989) 7 ACLC 52

Of course, this protection was subject to certain exceptions which limited the operation of the Rule in *Turquand's* case.

In *Northside Developments Pty Ltd v Registrar-General* [25] the High Court judges analysed the relationship between the Rule in *Turquand's* case and the general agency principles in different terms. In particular, Dawson J [26] considered that the Rule depended on the operation of agency law. The person who purported to act on behalf of the company must act within his actual or apparent authority.

The organic theory is also subject to agency rules. It is a principle of company law which attributes certain acts to be the acts of the company itself. In this way, a distinction is drawn between the acts of an agent which are binding on a company as a principal and acts which are directly those of the company. The affixing of the company seal has historically been regarded as a direct act of the company, generally through its board of directors and is analogous to the signature of a natural person. This theory also finds expression in relation to a company's liability in tort, criminal liability and the division of powers between the board and general meeting of members.

A company will only be bound by its own act where the persons acting as the company do so within their actual or apparent authority. The organic theory merely extends the scope of the capacity of an agent to bind the company directly.

25 (1990) ACLC 611 at p 645

26 Ibid

It does not enable a person who acts without authority to bind the company. This includes the situation where the company seal is affixed.

Toohey J[27] stated that the Rule in *Turquand's* case originally evolved in relation to irregularities in the internal management of companies, such as failure to hold proper meetings or pass regular resolutions. The issues which arise where officers of a company act without authority are resolved by application of agency rules rather than indoor management in the strict sense. While the Rule in *Turquand's* case protects outsiders where there is an irregularity it does not extend to confer authority on an officer where that authority does not otherwise exist. This is apparent from the *Freeman and Lockyer v. Buckhurst Park Properties (Mangal)Ltd*[28]. and *Crabtree-Vickers Pty. Ltd. v. Australian Direct Mail Advertising and Addressing Co. Ltd.*.[29]

Mason CJ[30] considered that the Rule in *Turquand's* case is a particular aspect of the principles of agency law. It is unclear whether agency principles extend to a presumption of regularity where the common seal has been affixed. In such a case, the organic theory may operate separately from the law of agency. The affixing of the company seal represents corporate assent arising from a resolution of the board which is the appropriate organ of the company.

---

[27] *Northside Development Pty. Ltd. v. Registrar General* (1990) 8 ACLC 611

[28] [1964] 2 QB 480 (Court of Appeal, England)

[29] (1975) 133 CLR 72 (High Court of Australia)

[30] *Northside Development Pty. Ltd. v. Registrar General* (1990) 8 ACLC 611

Brennan J[31] considered that the Rule comes within the framework of apparent authority which itself is based upon estoppel. The company is prevented from denying the representation of authority which it has made. There is no material distinction between acts of natural persons in affixing the company seal which are acts of the company itself or acts of an agent of the company. The principles established in the *Freeman and Lockyer* and *Crabtree-Vickers* cases are applicable to cases involving the Rule in *Turquand's* case.

Gaudron J[32] thought that the principles of apparent authority represent an example of estoppel. The rule in *Turquand's* case is also based on principles which provide the foundation of estoppel.

4.3 Exception to the Rule in Turquand's Case

In Malaysia, the Rule in T*urquand's* case is applied with its common law exceptions. The exceptions limit the outsiders ability to rely upon the Rule.

The exceptions to the Rule in T*urquand's* case are:

i) if the contracting party knows or should know of the agents lack of authority he cannot rely on the Rule in *Turquand's* case. This is usually the case where the contracting party is an "insider", that is, a person who by virtue of his position should know of the incapacity. This is illustrated in the case of *Howard v. Patent Ivory Manufacturing Co.*[33]. In the case the directors of the

---

[31] Ibid at p.611

[32] *Northside Development Pty. Ltd. v. Registrar General (1990) 8 ACLC 611*

[33] *(1888) 38 ChD 156*

company lent money to the company on the security of debentures. The articles of association provided that the company could only borrow up to a certain limit, and this limit has been exceeded. The directors sought to enforce the debentures. The court declined to let them do so. They were all directors of the company; as directors they knew or should have known of the limitation of borrowing. Accordingly, they could not rely upon the rule in *Turquand's* case.

However, the fact that one party to the contract is the director of the company himself does not automatically mean that he cannot take advantage of the Rule. It all depends whether he ought to have known of the agents lack of authority.[34]

ii) if there are circumstances that would put the contracting party on inquiry, the Rule in *Turquand's* case will not apply.[35] Sometimes the circumstances are such that a reasonable man would be suspicious of the agent's authority; if this is so, the contracting party must make reasonable inquiries. If such inquiries would have revealed the agent's lack of authority, the contracting party cannot rely on the Rule in *Turquand's* case to assist him.[36]

---

[34] *Hely- Hutchinson v. Brayhead Ltd. [1968] 1QB 549, 578 – 579*

[35] *B Liggett (Liverpool) Ltd. v. Barclays Bank Ltd. [1928] 1 KB 48*

[36] *Progress Advertising (NZ) Ltd. v. Auckland Licensed Victuallers Industrial Union of Employers [1957] NZLR 1207, 1213 (Supreme Court of New Zealand)*

Lord Simonds in *Morris v Kanssen* stated,

> "he cannot presume in his own favour that things are rightly done if inquiry that he ought to have made would tell him that they were wrongly done". [37]

Lord Esher MR expressed this inferred actual knowledge in *English and Scottish Mercantile Investment Co Ltd v Brunton,* [38]

> "When a man has statements made to him, or has knowledge of facts, which do not expressly tell him of something which is against him, and he abstains from making further inquiry because he knows what the result would be - or, as the phrase is, he 'wilfully shuts his eyes' - then judges are in the habit of telling juries that they may infer that he did know what was against him. It is an inference of fact drawn because you cannot look into a man's mind, but you can infer from his conduct whether he is speaking truly or not when he says that he did not know of particular facts".

In *Northside Developments Pty Ltd v Registrar - General* [39] all five judges of the High Court held that a bank was put on inquiry where it sought to enforce a mortgage against a company. It was put on inquiry as to the authority of the persons who affixed the company seal to the mortgage document. This was because of the nature of the transaction which was firstly of no benefit to the

[37] [1946] AC 459 at p 475

[38] [1892] 2 QB 700 at p 707-8

[39] (1990) 8 ACLC 611

company and secondly, appeared unrelated to its business. It secured debts of companies controlled by the person who signed as director but these companies has no association with the company against which the bank sought to enforce the mortgage. The inquiry exception was triggered because the bank took no steps to establish that the company's officers had authority to affix the company seal. Therefore, if a person knew the truth or he ought to have known the truth, he cannot rely on the Rule.

iii) if an examination of the company's memorandum or articles of association would have made it plain that the agent's authority was limited, the contractor may not depend in the Rule in *Turquand*'s case. This can be enunciated from the case of *Irvine v. Union Bank of Australia*[40] . A party cannot plead that he has not actually read the memorandum or articles of association since everyone is deemed to have constructive notice of those documents.[41] This only applies if it is clear from the memorandum and articles of association that the agent could not authorise or that the contractor was put on inquiry by reason of some provision of the memorandum and articles.[42] If the memorandum and articles envisage the agent may be so authorised subject to some prescribed formalities being satisfied, the Rule in *Turquand's* case applies in full force and the contractor need not inquire further.

---

[40] (1877) 2 App Cas 366 (Privy Council on appeal from Burma)

[41] *Ernest v. Nicholls (1875) 6 HL Cas 401; Woodland Development Sdn. Bhd. v. Chartered Bank [1986] 1 MLJ 84, 88 –89.*

[42] *Rolled Steel Products (Holdings) Ltd. v. British Steel Corp. [1984] BCLC 466.*

iv) as it is often stated that the Rule in *Turquand's case* has no application where forgery is involved. This idea appears to stem from the decision of the House of Lords in *Ruben v, Great Fingall Consolidated*[43].

However, forgery may arise in two senses. In the strict sense it is as illustrated in *Ruben 's case,* where a false or counterfeit seal or signature is affixed. In this case the forgery is a nullity and cannot be binding on the company, so it therefore falls outside the Rule. Forgery may arise in a wider sense where the seal and signatures are genuine but affixed by persons acting without authority. In such cases, the Rule in *Turquand's* case does not apply where the officers lacked actual or apparent authority.

Mason CJ in the *Northside Development* case expressed doubt on whether forgery is a true exception to the Rule in *Turquand's* case. This question did not have to be resolved in the *Northside Development* case because of the operation of the inquiry exception. In any case, he said that the forgery exception has a narrow area of operation. This appears to refer to the distinction between cases where the company seal and signatures are forged and those where the seal and signatures are genuine but are fixed without authority.[44] Mason CJ appears to imply that only forgery in the strict sense is an exception to the Rule in *Turquand's* case.

Brennan J also considered that "forgery" may be used in both senses. In the strict sense where a false seal or signature is affixed, this is outside the Rule in

[43] [1906] A.C. 439

[44] Example of the latter type of forgery may be seen in *Kreditbank Cassel GmBH v. Shenkers* [1972] 1 KB 826

Turquand's case because the Rule is based on estoppel and the company is not estopped in such cases of forgery. In the wider sense the relevant question is whether the persons who affixed the seal had authority from the company to do so.

Despite the differences between the judges it may be possible to indicate circumstances where forgery may result in an outsider losing the entitlement to rely on the Rule in *Turquand's* case. In the case of a counterfeit seal or signatures and in the wider sense of forgery, the relevant question comes back to whether the company held out the persons who affixed the seal as having authority to do so.

This raises issues under general agency law dealing with the creation of actual or apparent authority. In the Australian case of *Storey v Advance Bank Australia Ltd*[45], a signature of a director was forged on the affixing of the seal to a mortgage. The mortgage was held to be valid despite the forgery because the director with whom the bank dealt was permitted de facto control over the company's business by the director whose signature was forged.

4.4 The English Position

In England, the statutory changes discussed in Chapter 2, that is, ss.35, 35A and 711 of the Companies Act 1985 and s.322A of the Companies Act 1989 drew the sting

[45] (1993) 11 ACLC 629

of the ultra vires and constructive notice, thus improving the outsiders position in relation to its dealings with the company.

However s.35 of the Companies Act 1985 helps the outsider dealing with the employee of the company only to the extent that he may safely assume that the board had the power to delegate to that employee. It will not protect him unless the board has actually done so or is estopped from denying that it has or has ratified what he did. If it has not, he will be unprotected unless the employee has acted within his apparent authority; and he will lose that protection not only if he has not acted in good faith but also if he has negligently failed to make proper inquiries or if he actually knew or ought to have known that the officer exceeded his authority.

4.5 Conclusion

The Rule has been criticised because of uncertainty which has arisen from a large body of case law. Professor Gower observed:

> " Unhappily its obscurity increases in direct proportion to the literature upon it, and only its undoubted practical importance makes it essential to devote some space to it even at the risk of further obfuscation."

Gower commented that the history of the development of the Rule saw an increase in the limitations to which the rule was subject. These limitations have become so extensive that the object of the rule has been obscured.

" The result is that the law has become a jungle of irreconcilable decisions to the benefit of no one save the legal profession. If this branch of the law is ever codified the draftsman will be well advised to ignore all case law of the present century and to go back to the first principles and the judgments of the founding fathers of our modern company law. Unhappily a textbook writer has to state the law as he finds it and not as it ought to be."[46]

As a consequence, in Australia, the common law principles discussed above have been now been replaced by statutory provisions. The following chapter will discuss these statutory provisions in detail.

[46] Thompson "Company Law" Doctrines and Authority to Contract (1956) Univ of Toronto LJ 248 at p 254

CHAPTER 5

THE AUSTRALIAN POSITION

5.1 INTRODUCTION

Detailed treatment is given in this chapter to developments in Australia because it is the most extensive statutory development in the Commonwealth on the subject of this dissertation in recent years.

In Australia, the common law principles discussed in Chapter 4 have now been replaced by statutory provisions contained in ss. 164 to 166 of the Corporations Law (herein after referred to as the 'Corporation Law'). These provisions are based around six protective assumptions set out in s.164(3) of the Corporation Law and are subject to the limitations in s.164 (4).This chapter will also consider the extent to which the statutory provisions in Australia could be adopted in Malaysia.

5.2 Sections 164 – 166 of the Corporation Law

S.164 (1) and (2) of the Corporation Law lays down that a person having dealings with a company or with a person who has acquired property from a company is able to make the assumptions of regularity concerning the indoor management of a company. These assumptions are binding on the company which is unable to assert that particular assumptions are incorrect and should be disregarded.

The provisions of the Corporation Law relevant to this chapter are s.164(3), s.164(4), s.165 and s.166. It is necessary to cite the sections in full to appreciate their impact and

for a proper understanding of the discussion which will follow. Section 164(3) deals with persons who are entitled to make certain assumptions. The provision reads:

> The assumptions that a person is, by virtue of subsection (1) or (2), entitled to make in relation to dealings with a company, or in relation to an acquisition or purported acquisition from a company of title to property, as the case may be, are:
>
> (a) that, at all relevant times, the company's constitution has been complied with;
>
> (b) that a person who appears, from notices or returns lodged under section 242 or 335 or with a person under a previous law corresponding to section 242 or 335, to be a director or a secretary of the company has been duly appointed and has authority to exercise the powers and perform the duties customarily exercised or performed by a director or by a secretary, as the case may be, of a company carrying on a business of the kind carried on by the company;
>
> (c) that a person who is held out by the company to be an officer or agent of the company has been duly appointed and has authority to exercise the powers and perform the duties customarily exercised or performed by an officer of the kind concerned;
>
> (d) that an officer or agent of the company who has authority to issue a document on behalf of the company has authority to warrant that the document is genuine and that an officer or agent of the company who has authority to issue a certified copy of a document on behalf of the company has authority to warrant that the copy is a true copy;

(e) that a document has been duly sealed by the company if it bears what appears to be an impression of the company's seal and either :

(i) the sealing of the document appears to be witnessed by 2 people, one of whom may be assumed to be a director of the company because of paragraph (b) and (c) and the other of whom may be assumed to be a director or a secretary of the company because of those paragraphs: or

(ii) the sealing of the document appears to be witnessed by one person who may be assumed to be a director and a secretary of the company because of paragraph (b): or (c) but only if it is stated next to the signature that the person witnesses the sealing in the capacity of sole director and sole secretary of the company; and

(f) that the directors, the secretaries, the employees and the agents of the company properly perform their duties to the company.

Section 164(4) deals with the exceptions to s.164(3) and the provision reads:

Despite subsection (1), a person is not entitled to make an assumption referred to in subsection (3) in relation to dealing with a company if:

(a) the person has actual knowledge that the matter that, but for this subsection, the person would be entitled to assume is not correct; or

(b) the person's connection or relationship with the company is such that the person ought to know that the matter that, but for this subsection, the person would be entitled to assume is not correct;

and where, by virtue of this subsection, a person is not entitled to make a particular assumption in relation to dealings with a company, subsection (1) has no effect in relation to any assertion by the company in relation to the assumption.

S.165(1) abolishes the doctrine of constructive notice. The section reads:

Subject to subsection (2), a person shall not be taken to have knowledge of:

(a) a company's memorandum or articles or any of the contents of a company's memorandum or articles;

(b) a document or the contents of a document; or

(c) any particulars;

merely because of either or both of the following:

(i) the memorandum, the articles, the documents or the particulars has or have been lodged with the Commission, or lodged with a person under a previous law corresponding to a provision of this Law;

(ii) the memorandum, the articles, the document or the particulars is or are referred to in any other document that has been lodged with the Commission, or lodged with a person under a previous law corresponding to a provision of this Law

S.166 allows the outsider to rely on s.164(3) assumptions even if an officer, agent or employee of the company commits fraud. The provision reads:

(a) to entitle a person to make the assumption referred to in subsection (3) of that section in relation to dealings with a company; or

(b) to entitle a person to make the assumptions referred to in subsection (3) of that section in relation to an acquisition or purported acquisition (whether direct or indirect) of title to property from a company;

even if a person referred to in paragraph 164 (3) (b), (c) or (e) or an officer, agent or employee of the company referred to in paragraph 164 (3) (d) or (f) acts fraudulently in relation to the dealings or has forged a document that appears to be sealed on behalf of the company.

The Explanatory Memorandum to the Companies and Securities Legislation (Miscellaneous Amendments) Act 1983 said that the purpose behind the s.164(3) assumptions is to:

"ensure that a person who deals in good faith with persons who can be reasonably supposed to have the authority of the company should be protected against later claims by the company that the persons purporting to act for it lacked authority. This involves clarifying and codifying the so-called 'indoor management rule' which has developed from the decision in *Royal British Bank v Turquand* [1].

The Explanatory Memorandum considered that the state of case law was not entirely clear or satisfactory despite the considerable amount of litigation revolving around the Rule in *Turquand's* case.

It was clear from the Explanatory Memorandum, that the dominant policy consideration behind ss164 - 166 is to protect outsiders acting in good faith. As will be seen below, most of the cases interpreting this legislation have concerned the issue of whether the

[1] (1856) 119 E.R. 886.

outsider ought to be excluded from entitlement to gain that benefit of the protective assumptions.

The assumptions sought to codify and clarify the Rule in *Turquand's* case. Gummow J in *Australian Capital Television Pty Ltd v Minister for Transport and Communications*[2], considered that s.164 was not a "comprehensive code" but designed to repair the failings of the common law. Kirby P said that s.164 does not appear in a legal, social and economic vacuum. It does not override the principles and policies of the common law unless this is plainly the result intended by the legislation[3]. Kirby P did not think that it was a universal and unconditional objective of the legislation to protect persons dealing with a company at the expense of all other competing considerations. Its purpose is to protect such persons who deal in good faith and innocently. Kirby P thought that the competing policy considerations behind the Rule in *Turquand's* case as stated by Mason CJ in *Northside Developments Pty Ltd v Registrar-General*[4], are also applicable in the interpretation of s.164 of the law.

The strict interpretation of the reference in s.164 (1) to "a person having dealings with a company" would remove the benefit of the assumptions from an outsider who is unable to show the existence of an actual pre-existing legal relationship with the company.

The term "dealings" was given a broad meaning in *Storey v Advance Bank Australia Ltd*[5].In this case, a bank dealt with a managing director who was permitted de facto control of the conduct of a company's business by the other director. It was held that the

---

[2] (1989) 7 ACLC 525

[3] *Bank of New Zealand v. Fiberi Pty.Ltd.* (1994) 12 ACLC 48 at p.51

[4] (1990) 8ACLC 61

[5] (1993) 11 ACLC 629

concept of having dealings with a company extends beyond dealing with someone who has actual authority and includes situations where a document is forged. It extends to purported dealings.

Ford and Austin suggest that the expression should be interpreted so as to enable the assumptions to apply where the outsider reasonably believes that dealings were conducted with the company through a person who may be supposed to have a connection with the company appropriate to the particular dealings[6]. This interpretation would enable an outsider to be protected in cases where the outsider is unable to show that the company's agent possessed authority so as to bind the company. The company would then be unable to argue that the outsider did not have dealings with it but only with its officers or agents.

In *Brick and Pipe Industries Ltd v Occidental Life Nominees Pty Ltd* [7] it was held that each of the assumptions in s 164 (3) of the law is separate and discreet. This means that just because an outsider cannot rely on a particular assumption, he or she is not prevented from relying on the other assumptions. While the assumptions are discreet, they may overlap and an outsider may rely upon more than one assumptions: *Bank of New Zealand v Fiberi Pty Ltd*[8].

It is not necessary for an outsider to actually make these assumptions in order to rely upon them. In *Lyford v Media Portfolio Ltd*[9], a company argued that evidence showed that the making of the assumptions would have been contrary to the usual practice of the

---

[6] HAJ Ford and R P Austin Ford's - Ptrinciples Corporation Law 7th ed Butterworths

[7] (1992) 10 ACLC 253

[8] (1994) 12 ACLC 48

[9] (1989) 7 ACLC 271

concept of having dealings with a company extends beyond dealing with someone who has actual authority and includes situations where a document is forged. It extends to purported dealings.

Ford and Austin suggest that the expression should be interpreted so as to enable the assumptions to apply where the outsider reasonably believes that dealings were conducted with the company through a person who may be supposed to have a connection with the company appropriate to the particular dealings[6]. This interpretation would enable an outsider to be protected in cases where the outsider is unable to show that the company's agent possessed authority so as to bind the company. The company would then be unable to argue that the outsider did not have dealings with it but only with its officers or agents.

In *Brick and Pipe Industries Ltd v Occidental Life Nominees Pty Ltd*[7] it was held that each of the assumptions in s 164 (3) of the law is separate and discreet. This means that just because an outsider cannot rely on a particular assumption, he or she is not prevented from relying on the other assumptions. While the assumptions are discreet, they may overlap and an outsider may rely upon more than one assumptions: *Bank of New Zealand v Fiberi Pty Ltd*[8].

It is not necessary for an outsider to actually make these assumptions in order to rely upon them. In *Lyford v Media Portfolio Ltd*[9], a company argued that evidence showed that the making of the assumptions would have been contrary to the usual practice of the

---

[6] HAJ Ford and R P Austin Ford's - Ptrinciples Corporation Law 7th ed Butterworths

[7] (1992) 10 ACLC 253

[8] (1994) 12 ACLC 48

[9] (1989) 7 ACLC 271

outsider in making loans, therefore the assumptions could not be made. Nicholson J dismissed this argument on the basis that s.164 (1) of the Law prevents a company from asserting that any of the assumptions are incorrect. This is so, whether or not the assumptions were actually made by the outsider.

5.2.1 Compliance with memorandum and articles - s.164 (3) (a) of the Corporation Law

This assumption, contained in s.164 (3) (a) of the Corporation Law, is a restatement of the Rule in *Turquand's* case. However it appears to have a wider operation because the Rule in *Turquand's* case was subject to the doctrine of constructive notice which has now been abolished by s.165 (1) of the Corporation Law. Outsiders are no longer taken to be aware of provisions in the memorandum and articles. This enables outsiders to make the assumption that the company has complied with its memorandum and articles even though the memorandum and articles have not been complied with and this would have been apparent to the outsider had they been read. For example, if the articles contain a requirement that the company seal be used in every document acknowledging a debt, an outsider who is unaware of the articles is not taken to know of this requirement. In fact, the outsider can assume that the board has done all that is required to borrow the money.

This broader operation of the statutory assumption arising from the abolition of the doctrine of constructive notice has significant implications. It places an outsider who is unwilling to read the company's articles in a stronger positions than one who makes an effort to read the articles. This may sometimes unfairly advantage an outsider who deliberately dons blinkers in circumstances where there are grounds for suspicion that an

officer or agent of a company is acting in an unauthorised manner. This situation is also addressed by the limitations to the assumptions contained in s.164 (4) of the Law.

5.2.2 Where a person is named as an officer in certain public documents - s.164 (3) (b) of the Corporation Law

This assumption, contained in s.164 (3) (b) of the Corporation Law, operates where a person is named in the company's annual return under the Corporation Law. An outsider may assume that the named person does in fact occupy the stated position, has been duly appointed and has the authority to exercise the powers customarily exercised by a person occupying that position in a company carrying on a business of the kind carried on by the company.

By naming certain persons as being its officers in the annual returns, a company is holding out that those persons are officers occupying the stated positions with authority which is customary for such officers. In banking and other lending situations, this is probably the most important assumption because usual banking procedures involve a check of the company's returns in order to ascertain who are the officers of the company.

The operation of the assumption contained in s.164 (3) (b) of the Corporation Law was illustrated in *Re Madi Pty Ltd*[10]. A subsidiary company entered into a deed of guarantee in which it guaranteed repayment of loans made to its holding company. The company seal was affixed to the deed attested by a director and a person who signed as secretary.

---

[10] (1987) 5 ACLC 847

The company later claimed that it was not bound by the deed of guarantee because the person who signed as secretary had not been appointed despite having been named as one of two company secretaries at the relevant time. It argued that it was not bound because the seal had not been affixed in accordance with the articles. The Victorian Supreme Court of Australia held that the company was bound because the person had been named as secretary in the return lodged under the Companies Code (the predecessor to the Corporation Law). This amounted to a holding out by the company that the named person was its secretary and thereby authorised to affix the company's seal. This case illustrates that the s.164 (3) (b) of the Law assumption departs from the common law agency rules. The apparent authority of an agent depends upon a representation that the person has authority and reliance by the outsider upon this representation[11]. Under s.164 (3) (b) of the Corporation Law, the outsider may be totally unaware of the particulars contained in the annual returns and therefore cannot be said to rely upon this information. Nevertheless the company will be bound by the representation contained in the return.

The s. 164 (3) (b) assumption appears to be unnecessarily narrow in that it refers only to returns lodged under the Corporation Law. The law usually requires certain other documents to be filed which are equally open to public inspection. In *ANZ Banking Group Ltd v Australian Glass and Mirrors Pty. Ltd.* [12] a bank sought to rely on a form which listed the persons who consented to act as directors. This was the only form filed by the company at the relevant time prior to execution of a mortgage debenture as the company was newly incorporated. The company had not lodged returns under the

---

[11] *Freeman & Lockyer v.Buckhurst Park Properties (Mangal) [1964] 2 QB 480 per Diplock LJ*

[12] (1991) 9 ACLC 702

Corporation Law, however the bank could not rely on the filed form for the purposes of s.164 (3) (b).

It is unclear what purpose is served by so distinguishing between forms or documents required to be lodged. It might be more practical if s.164 (3) (b) of the Corporation Law is to be enacted in Malaysia that it be expanded so as to allow outsiders to rely on any forms or documents which are lodged.

However, it must be stated that the filing of forms other than in accordance with the Law may constitute a "holding out by the company" for the purposes of the s.164(3) (c) assumption. This occurred in the *Australian Glass and Mirrors* case discussed above. This may not assist an outsider in cases where the company file was not actually searched. In such cases, the outsider could not be said to have relied upon the information contained in the filed form and therefore may not be able to assert that the agent of the company acted with apparent authority[13]. Reliance on a representation is a requirement for a holding out by the company under the principles stated in the *Freeman and Lockyer* case.

The policy objective of the legislation is to protect outsiders who act in good faith where a company seeks to avoid its actual contractual obligations by reliance on its own non-compliance with its memorandum or articles or obligations under the legislation. This

[13] *Lyford v Media Portfolio Ltd* (1989) 7 ACLC 271 however held that an outsider need not actually make the s.164 (3) assumptions in order to rely upon them. This would appear to modify the common law rules. However it is unclear whether there has been a holding out by the company where the outsider did not rely on such a representation.

would be better served by expanding the s.164 (3) (b) assumption to include any lodged document.

As is the case with the assumption under s.164 (3) (c), an outsider is entitled to assume that the particular officer of the company has the customary authority of the particular officer concerned. There is however, a difference in the wording of the assumptions in s.164 (3) (b) and (c). As discussed below, under s.164 (3) (c), an outsider may assume that the person held out by the company to be an officer or agent has the customary authority of an officer of the kind concerned. On the other hand, s.164 (3) (b) of the Law entitles an outsider to assume that a person named as an officer in the specified returns has the customary authority of an officer of a company carrying on a business of the kind carried on by the company.

5.2.3 Where a person is held out as an officer of agent s.164 (3) (c) of the Corporation Law

Outsiders, when dealing with an officer or agent of the company, are generally not aware of the extent of the actual authority of the agent. This is because actual authority stems from the principal-agent relationship and outsiders are rarely privy to this. It is much more common for the outsider to gain the impression that a particular person has authority to bind the company from the representations or conduct of the company itself or of persons acting as the company or on behalf of the company. Such representations or holding out create an agency relationship which binds the company by apparent or ostensible authority. These situations are governed under the law of agency which forms the basis of the protective assumptions contained in s.164 (3) (b) and (c). The s.164 (3) (b) assumption operates where the representation takes the form of naming a person as an

officer in certain returns filed with the Australian Securities Commission. The s.164 (3) (c) assumption operates where the holding out by the company arises in other ways.

The agency principles of apparent authority in Australia have been restated by the statutory assumptions contained in s.164 (3) (b) and (c).

Under s.164 (3) (c), a person having dealings with a company is entitled to make the assumption that a person who is held out by the company to be an officer or agent of the company has been duly appointed and has authority to exercise the powers and perform the duties customarily exercised or performed by an officer or agent of the kind concerned.

This assumption comprises two main elements which must be established by the outsider:

i) a holding out or representation by the company that a person is an officer or agent; and

ii) the particular power exercised by this person is within the scope of powers customarily exercised or performed by an officer or agent of the kind concerned.

The purpose of this assumption was stated in the Explanatory Memorandum to be a restatement of the protection given to outsiders under the "indoor management rule" where the company's officers and agents have not been properly appointed[14]. This protection was given to an outsider at common law[15].

---

[14] Para 205

[15] *Mahoney v East Holyford Mining Co* (1875) LR 7 HL 869

The statutory assumption does away with the distinction drawn between defective appointments and non-existent appointments. This distinction was drawn by the House of Lords in *Morris v Kanssen*[16] in the context of interpreting the equivalent of s.226 of the Companies Act 1985. This section validates contracts where directors or a secretary of a company act despite a defect in their appointments. The acts of directors or secretary are valid notwithstanding any defect that may afterward be discovered in their appointment or qualification. Such acts are not validated under s.226 where there has not been an appointment at all.

5.2.3.1. What is a "holding out by the company"?

The first element of the s.164 (3) (c) assumption requires that a person is held out by the company to be an officer or agent of the company. In order to gain the protection of this assumption, it would appear that an outsider must establish the creation of apparent authority in the same way as under the agency rules applied in the *Freeman and Lockyer* and *Crabtree-Vickers* cases[17].In *Freeman and Lockyer v Buckhurst Park Properties (Mangal) Ltd*[18], Diplock J stated that several conditions must be met in order for an outsider to hold a company liable under a contract where the company's agent did not posses actual authority. In particular, a representation that the agent had authority must be made by a person or persons who had actual authority to manage the business of the company either generally or in respect of the particular contract concerned. In *Freeman and Lockyer* the representation was made by the board because it failed to prevent a person from acting as if he was the company's managing director.

---

[16] (1946) AC 459

[17] See *Bank of New Zealand v Fiberi Pty Ltd* (1994) 12 ACLC 48 per Kirby P at p 57

The question whether the person who made the representation of authority was able to make the representation for the company depends on whether that person has actual authority to do so. In *Crabtree-Vickers Pty Ltd v Australian Direct Mail Advertising & Addressing Co Pty. Ltd.*[19] such a representation was made by a person who acted as managing director but had not been formally appointed. Since this person did not have actual authority to manage the company's business, he was not capable of representing that someone else had apparent authority to enter into a contract on behalf of the company. The outsider was therefore unable to enforce a contract against the company.

This decision can be criticised on the basis that it does not give due regard to commercial practice. It exposes an outsider to uncertainty where a representation is made by someone who an outsider reasonably believes has authority but it turns out that the representation was not made by someone with actual authority "to manage the business of the company either generally or in respect of those matters to which the contract relates"[20]. It is often almost impossible for an outsider in a case such as *Crabtree-Vickers*[21] to discover who has actual authority to make representations for the company.

A more commercially realistic approach was taken by the court in *Brick and Pipe Industries Ltd v Occidental Life Nominees Pty Ltd* [22]. In this case a de facto managing director was taken to have implied actual authority to manage the business of the company. The person concerned had assumed a dominant position in control of the

---

[18] [1964] 2 QB 480

[19] (1976) 50 ALJR 203

[20] Diplock LJ at p 505-6

[21] Supra note 19

[22] (1992) 10 ACLC

company with the acquiescence of the other directors and his mind and will was attributed to the company itself. A representation by this person was a representation of the company and he could not hold out for the company that someone else had apparent authority in relation to a particular dealing.

Under the statutory provision, it is possible that a de facto managing director in the position which arose in *Freeman and Lockyer* would have apparent authority to bind the company as an agent in entering into a contract on behalf of the company but would not have implied actual authority to hold out for the company that someone else has authority to bind the company. Such a result does not appear to have been intended by the legislation which aims to protect outsiders who act bona fide. To require outsiders to ascertain whether the person with whom they are dealing has actual or apparent authority is to demand the type of inquiry into the internal workings of the company to which the Rule in *Turquand's* case applied to protect an outsider acting in good faith.

"A holding out by the company" would include acting through its members in general meeting or through its directors or through its principal executive, or through an officer or agent of the company. This highlights whose representations may be attributed to the company for the purpose of a "holding out by the company." It would also appear to encompass a representation made by a de facto managing director. "Principal executive officer" is defined in s.9 of the Corporation Law to include a person who may be called by another name or who may not even be a director. In most cases this will include a de facto managing director in circumstances which arose in the *Freeman and Lockyer* and *Crabtree-Vickers* cases.

Clearly, where the board makes a representation, this is a representation of the company under the organic theory. A representation made by a properly appointed managing director or committee of directors may be similarly seen where delegation by the board is permitted under the articles. Where the representation is made by a de facto managing director, this may come within the term "principal executive officers".

The uncertainty arises where the representation is made by an individual director. This also raises the question regarding the customary authority of an individual director. Generally, an individual director does not have the customary authority to make representations which are binding on the company. However, whether there has been a holding out by the company for the purposes of s.164(3)(c), constituted by a representation of a single director, depends upon the circumstances. In *Bank of New Zealand v Fiberi Pty Ltd*[23] it was held that an individual director did not have actual authority to hold out for the company in circumstances where the other director was unaware of the conduct of the representor and had not acquiesced to the conferral of this authority. This case differs from the *Brick and Pipe* case where the other directors acquiesced to the conferral of wide authority upon the director who made a similar representation. It appears that in order to gain the protection of s.164(3)(c) of the Corporation Law an outsider is required to look into whether the board has acquiesced to the conferral of actual authority. The position of an outsider is strengthened if steps are taken to ascertain the authority of the person with whom the outsider deals.

---

[23] (1994) 12 ACLC 48

In *ANZ Banking Group Ltd v Australian Glass and Mirrors Pty Ltd*,[24] a mortgage debenture under seal was executed by a company. The company seal was affixed and witnessed by the director and secretary. At the time of execution, those persons had not been appointed. The solicitor who had incorporated the company was still named as a director and a legal secretary was the other director and secretary. The company defaulted and the lending bank sought to enforce its security under the mortgage debenture. The company argued that the deed was unenforceable because the seal was affixed by persons who were not directors. Kaye J considered the circumstances which constituted a holding out for the purposes of s.164 (3) (c) of the Corporation Law by the company, that the persons who witnessed and affixed the seal of the company were authorised to act as directors at the time of execution. The filing of the form listing the persons who consented to act as directors were regarded as particularly significant. When the bank's solicitors conducted a company search prior to the execution of the mortgage debenture, it was the only form filed by the company. The filing of this form made it reasonable for the bank to assume that the persons who executed the mortgage debenture had been appointed as directors. As regards the persons who were named as directors at the time of execution of the mortgage debenture, it was reasonable for the bank to assume that the named directors and secretary were the solicitor and an employee who merely incorporated the company.

Other circumstances which indicated a holding out by the company were the past

---

[24] (1991) ACLC 702

dealings between the bank, the company and the persons who purported to be its directors. They had previously opened an account in the name of another company and had given personal guarantees. When this account was closed and a new one opened in the name of the defendant company, all negotiations were conducted by the same persons. They also stated on a signed form that they were authorised to sign cheques on behalf of the company and otherwise act in dealings between the bank and the company. The persons who purported to act as directors also signed personal guarantees and affixed the company seal on other documents.

It can be seen from this case that the position of the outsider was considerably strengthened by the fact that the bank had searched the company's file and discovered the form of consent to act as a director. Had the bank not searched the company file and been unaware that the consent to act form had been filed, it could possibly not be said that the company had held this out to the bank because the bank would not have been induced to enter into the contract by the filing of a form the existence of which it did not know.

It would seem that the position of an outsider who acts in good faith should be strengthened by expanding the operation of the s.164 (3) (c) assumption. A "holding out by the company" should be taken to include representations by an officer of the company who, it was reasonable in the circumstances for an outsider to believe, had authority to make the representation for the company. This may include representations by persons who did not have actual authority to make those representations. This would overcome the restrictive effect of the common law rules of agency as stated in the *Freeman and Lockyer* case and applied in *Crabtree-Vickers* case.

5.2.3.2. Reliance on Representation

In order for agency by apparent authority to arise at common law, it must be shown that the outsider was induced by the representation to enter into the contract and in fact relied upon it.[25] Without this reliance, the outsider may be unable to seek the protection of the common law rules of agency. The holding out by a company that a person has authority to act as its officer or agent must be made known to the outsider who must then act in reliance on the representation.

It appears that the common law rules of agency as stated in the *Freeman and Lockyer* case may have been modified by the s.164 (3) (c) assumptions.

In *Lyford v Media Portfolio Ltd*[26] it was held that an outsider need not actually make the assumptions contained in s.164 (3) of the Corporation Law in order to rely upon them. A company is prevented under s.164(1) of the Corporation Law from asserting that the assumptions are incorrect. It is not relevant that the outsider actually made the assumptions.

In *Brick and Pipe Industries Ltd. V Occidental Life Nominees Pty. Ltd* [27] ,the Full Court of the Supreme Court of Victoria approved the following statement of Ormiston J at first instance:

---

[25] *Freeman and Lockyer v Buckhurst Park Properties (Mangal) Ltd* [1964] 2 QB 480 at p 505.

[26] (1989) 7 ACLC 271

[27] (1992) 10 ACLC 253 at p 265

"...the section talks only of assumptions which may be made and need not necessarily reflect the actual assumptions made by the parties seeking to rely on s.164."

This appears to dispense with the common law requirement that the outsider must rely on the representation in order to hold the company bound by the acts of an agent who was held out by the company to be an officer or agent.

5.2.4 Customary Authority of Officers

The second element of s. 164 (3) (c) is that the person who has been held out by the company to be an officer or agent has authority to exercise the powers and perform the duties customarily exercised or performed by an officer of the kind concerned. This aspect involves a consideration of the customary authority of a company's officers, which would appear to incorporate the general agency rules in their application to companies.

It was enunciated in *Hely-Hutchinson v Brayhead*[28] that to be its managing director, that person has wide customary authority which is only limited in cases of unusual transactions. These limits were considered under the common law principles. In such cases, the protective assumptions may in any case be subject to the limitations contained in s. 164 (4) of the Corporation Law.

Where the person with whom the outsider deals is an ordinary director, the outsider is at

---

28 (1968) QR 549 at 583

the company than does an agent in relation to a principal. It is therefore more important to protect the interests of a principal in cases where an agent acts in an unauthorised manner. In the case of a company standing as a principal, the policy of the legislation is to hold the company liable for the acts of its officers. An outsider should not be deprived of reliance on the protective assumptions where the making of such assumptions is reasonable. The limitations contained in s.164 (4) of the Corporation Law are intended to operate in cases where the outsider does not act in good faith.

The customary authority of a company secretary is narrower than that of a director. While the role of the company secretary is far more important today than during the last century, the customary authority of the company secretary is restricted to contracts connected to the administrative side of a company's affairs.[31]

As discussed above, in *Northside Developments Pty Ltd v. Registrar-General*[32] , Dawson J held that a company secretary did not have apparent authority to affix the company seal to a document which mortgaged the company's land.

Ford and Austin[33] suggest that s.164 (3) (c) impliedly requires a consideration of the kind of business carried on by the company in determining the question of customary authority. This would be consistent with common law principles which may restrict the customary authority of a managing director to acts which are within ordinary trading

---

[31] *Panorama Development (Guildford) Ltd. v. Fidelis Furnishing Fabrics Ltd.* (1971) @QB 711 pp. 716-717

[32] (1990) 8 ACLC 611 at p 645.

[33] Note 2 at p. 545

transactions. It must be noted that the limits of this customary authority are uncertain.

5.2.5 Officers or agents have authority to warrant that documents are genuine - S.164(3)(d) of the Corporation Law

Under s.164(3)(d), a person dealing with a company may assume that an officer or agent of the company who has authority to issue a document on behalf of the company, has authority to warrant that it is genuine. Therefore a company secretary may be assumed to have the requisite authority to warrant that a share certificate is genuine. At common law it was doubtful whether a company secretary had authority to do this. Section 164(3)(d) of the Corporation Law overrules a principle stated in the case of *Ruben v. Great Fingall Consolidated*[34] . In that case, a company secretary forged a share certificate and purported to issue it on behalf of the company. The share certificate appeared to have been validly issued, however the company seal had been affixed without authority. Two directors' signatures had been forged and the company secretary had countersigned the certificate without authority. The secretary then lodged the certificate as security for a loan to himself. After the secretary defaulted, the lender was refused registration as owner of the shares and sued the company. He argued that the *rule in Turquand's* case operated so that he could assume that the internal proceedings of the company regarding the issue of the share certificates were properly carried out. The House of Lords held that the company was not bound by the forged certificate. It had not held out that the secretary had the authority to do more than merely deliver valid certificates. Therefore the lender

---

[34] [1906] AC 439

was not the true owner of the shares. While the authority of a company secretary has been considerably broadened since this case[35] , the authority of a secretary to warrant that a document that he or she has issued is genuine, has not been expressly considered. The s.164(3)(d) assumption specifically clarifies this position.

5.2.6 Assumption of Valid Sealing - S.164 (3) (e) Of the Law

The previous discussion regarding the assumptions dealing with the actual or apparent authority of a company's officers and agents is directly relevant to the question whether the affixation of the company's seal is binding on a company. Under s.164 (3) (e) of the Law, a person dealing with a company may assume that a document has been duly sealed if is bears what appears to be an impression of the seal of the company and the sealing appears to be attested by two persons, one of whom, by virtue of s.164 (3) (b) or (c) appears to be a director and the other appears to be either a director or secretary of the company.

This statutory assumption seeks to clarify the common law position. The uncertainty surrounding the law with respect to whether a company was bound by the affixing of the common seal was indicated by the different approaches taken by the High Court judges in *Northside Development Pty Ltd v Registrar-General.*[36]

Mason CJ considered that contracts under seal were different to contracts made by

---

[35] *Panorama Developments (Guildford) Ltd. v. Fidelis Furnishing Fabrics Ltd. [1971] 2 QB 711*

[36] (1990) 8 ACLC 611. The judgements of Mason CJ and Brennan J in this case were discussed in "The Rule in Turquand's Case: Past or Present?" (1991) 9 C&SLJ 37.

directors or officers of the company itself. The Rule in *Turquand's case*, when applied to contracts under the company seal, are an organic principle of company law rather than an application of agency law. The presence of the company seal has particular significance because it is indicative of,

> "corporate assent stemming from a resolution of the board of directors, the determinative act then being that of the board which is the organ of the company which administers its affairs."[37]

Even though in the *Northside case* there was no resolution of the board that the company seal can be affixed, the presence of the common seal nevertheless gave rise to the presumption that the seal had been affixed with the authority of the directors. An outsider dealing with a company could rely on the validity of the affixing of the common seal where it appears to be accordance with the articles.

Brennan J thought that there was no special significance in the fact that the contract was executed under the seal of the company. He said that,

> "It is immaterial whether the acts of natural persons in executing an instrument which binds the company are invested with the character of acts done by an agent of the company."[38]

---

[37] Ibid at p 620

[38] Ibid at p 626

The assumption contained in s.164 (3) (e) protects an outsider in circumstances where the common seal of a company was affixed by an officer or person held out by the company to be an officer where that person acted without authority. The operation of this assumption was illustrated in *Brick and Pipe Industries Ltd v_Occidental Life Nominees Pty Ltd.*[39] Brick and Pipe was taken over by a company controlled by Goldberg. The previous directors of Brick and Pipe were joined on the board by Goldberg and his son in law, Furst, and although remaining on the board, these previous directors ceased to take an active role in the management of the company. Another company controlled by Goldberg borrowed money form Occidental. This loan was secured by guarantees executed by thirteen other companies in the Goldberg group including Brick and Pipe. The deed of guarantee executed by Brick and Pipe was under the company seal which was attested by Goldberg and Furst as director and secretary respectively. The other directors had no knowledge of the existence of the guarantee and no board meeting was held to consider the transaction although minutes of such a supposed meeting were taken.

The lender's solicitor was aware that Furst had not been appointed as secretary. When this matter was raised, the financial controller of the Goldberg group said that the required appointment form had been lodged and stated that Furst was secretary and unauthorised to affix the company seal. This statement was made in front of Goldberg who acquiesced to it by remaining silent. After receiving this assurance, Occidental proceeded with the transaction. The Full Court of the Supreme Court of Victoria held that

---

[39] (1992) 10 ACLC 253

Occidental was entitled to assume that the deed was duly sealed under s.164 (3) (e) of the Corporation Law. The central issue was whether Furst had been held out by Brick and Pipe to be its secretary in accordance with s.164 (3) (c) of the Corporation Law. It was held that there had been a holding out through the implied conduct of Goldberg. While Goldberg had only been appointed as an individual director, his dominance of the company with the acquiescence of the other directors, enabled Goldberg to "speak" for the company and represent its mind and will. The court also held that s.164 (3) (e) of the Corporation Law does not require a signatory to hold the office indicated on the document. Furst had been appointed as a director, however he signed as secretary.

The court also pointed out that the use of the wrong designation may be relevant for the purpose of establishing whether the limitation contained in s.164 (4) (a) is applicable. If the outsider was aware of the incorrect designation, this may establish that the outsider had actual knowledge that the document was not duly sealed. This limitation was not applied in the *Brick and Pipe* case.

In *Bank of New Zealand v Fiberi Pty Ltd*,[40] the New South Wales Court of Appeal also considered the valid sealing assumption contained in s.164 (3) (e). It came to the opposite conclusion that the outsider was not entitled to rely on this assumption. The company, Fiberi, was owned by Doyle and Arnhold who were its director's equal shareholders. Arnhold was also the secretary. Fiberi guaranteed debts of Doyle's companies and

---

[40] (1994) 12 ACLC 48.

granted a mortgage over land held by it to secure the guarantee. The company seal of Fiberi was attested by Doyle as director and his son as secretary, a position to which he had not been appointed. Arnhold knew nothing of the guarantees and mortgage.

Kirby P in the above case considered the operation of the s.164 (3)(e) assumptions and held that the lender could not rely on s.164 (3) (e) of the Corporation Law. This assumption of valid sealing incorporated the apparent authority assumptions contained in s.164 (3) (b) and (c). The common law principles of agency were applicable in determining whether there had been a holding out by the company.

On the basis of *Crab-Tree Vickers Pty Ltd v Australian Direct Mail Advertising and Addressing Co Pty Ltd*,[41] only a person with actual authority of the company could hold out others as a director or secretary. Kirby P in the *Bank of New Zealand case* held that the director had no authority to hold out for the company that his son was the company's secretary. A single director does not usually have the customary authority to hold out that a person is vested with authority to bind the company.

The company's solicitor also did not usually have this power. This conclusion is interesting because it is common for banks to seek statements from company solicitors regarding the authority of company officers.

In *ANZ Banking Group Ltd v Australian Glass and Mirrors Pty Ltd*[42] , Kaye J held that

---

[41] (1976) 50 ALJR 203.

[42] (1991) 9 ACLC 702.

s.164 (3) (e) entitled an outsider to assume that the affixing of the company seal by persons who had not been appointed as directors and secretary of a company had been validly affixed. This was because the company had held out that the persons concerned were officers of the company under s.164 (3) (c) and were authorised to affix the common seal. This holding out occurred with the lodgement of a return of a list of persons who consented to be directors. There had also been previous dealings which created this impression.

The statutory assumption of valid sealing clarifies the uncertainties of the Rule in *Turquand's case* apparent from the judgements in the *Northside case*. The validity of the affixing of the seal depends upon the authority of the company's officers as is the case with any other contract. This approach rebuts the suggestion of Mason CJ[43] in the *Northside case* that contracts under seal are different to other contracts because such contracts are acts of the company itself and the organic theory of company law is applicable rather than agency law. It is in accordance with the view of Brennan J in the *Northside case* who thought that there was no special significance in the fact that the company seal was affixed to a contract. The validity of the contract depended on the application of agency rules.[44]

5.2.7 Assumption of Proper Performance of Duties – S.164 (3) (f) Of The Law

Under the assumption contained in s.164 (3) (f) of the Law, a person dealing with a

---

[43] (1990) 8 ACLC 611 at p 620

[44] (1990) 8 ACLC 611 at p 626.

company is entitled to assume that the directors, the principal executive officer, the secretaries, employees and agents of the company properly perform their duties to the company.

According to the Explanatory Memorandum, this statutory presumption of regularity restates the common law principle enunciated in *Richard Brady Franks Ltd v Price*[45] This case involved an issue of debentures to persons including directors of the company. The validity of the debentures was challenged on the grounds that the issue was not authorised by a quorum of directors who were entitled to vote. The holders of the debentures were protected from the assertion by the company that the persons purporting to act for it lacked authority. Dixon J stated this rule.

> "Under the general law of agency it is a breach of duty for an agent to exercise his authority for the purpose of conferring a benefit on himself or upon some other person to the detriment of his principal. But, at the same time, if his act is otherwise within the scope of his authority it binds the principal in favour of third parties who deal with him bona fide and without notice of his fraud... The rule, no doubt, is the same with respect to the acts of directors. It follows that a transaction carried out by directors for their own or some other person's benefit and not to further any purpose of the company is voidable but not void."

---

[45] (1937) 58 CLR 112. See also *Hambro v Burnand [1904] 2 KB 10 and Lloyds Bank Ltd v The Chartered Bank of India, Australia and China [1929] 1 KB 40.*

by other means. This approach appears consistent with the other assumptions of s.164 (3) of the Corporation Law as it represents a part of the Rule in *Turquand's* case, enabling a presumption of regularity in the internal workings of the company.

The adoption of this broad meaning of "duties" enables an outsider to seek the protection of the assumption in s.164 (3) (f) where the company's officers or agents act beyond the authority conferred on them by the company. The outsider will only be precluded from relying on this assumption if he possess the knowledge referred to in the s.164 (4) limitations.

5.3 The Limitations to the Statutory Assumptions

The assumptions set out in s.164 (3) of the Corporation Law are subject to two limitations contained in s.164 (4) of the Law. These limitations prevent a person dealing with a company from making the statutory assumptions where the person has actual knowledge that the assumption is not correct or the person's connection or relationship with the company is such that the person ought to know that the assumption is not correct.

The Explanatory Memorandum, in introducing s.164(4) of the Corporation Law stated that the purpose of these limitations was "to make it clear that the protection afforded by the 'indoor management rule' is only available to 'innocent' parties"

The two limitations contained in s.164 (4) differentiate between situations where the

person dealing with the company has no "connection or relationship" with the company and where there is such a connection or relationship. In the latter case, the protective assumptions are lost where the person dealing with the company ought to know of circumstances that would indicate that the assumptions are incorrect.

The operation of these limitations to some extent serves the same purpose as the common law exceptions to the Rule in *Turquand's case*, because they prevent a person dealing with a company from assuming that the indoor management of a company is regular. They play a crucial role in determining the balance of interests between commercial convenience on the one hand and discouragement of fraud and unauthorised acts by officers and agents on the other. Of particular importance here is the extent to which the statutory limitations in s.164 (4) differ from the common law exception to the Rule in *Turquand's case* where the outsider has knowledge or put upon inquiry.

5.3.1 The "Actual Knowledge" Limitations

A strict reading of s.164 (4) (a) of the Corporation Law would indicate that this limitation is significantly narrower than the common law exception which puts outsiders on inquiry. The Full Court of the Supreme Court of Victoria agreed to this interpretation in the *Brick and Pipe case* by stating:

> "The expression 'actual knowledge' means, what we think it says. It does not lend itself to definition or elaboration."[49]

---

[49] (1992) 10 ACLC 253 at p 264.

However the Full Court of the Supreme Court implicitly recognised circumstances like in the fact situation which occurred in *Northside case.* In applying the common law rules, all members of the High Court held that in the circumstances, the lending bank was put on inquiry and therefore could not rely on the protection of the Rule in *Turquand's case* because it had not made further inquiry when its suspicions of irregularity should have been aroused. Under the statutory provisions, a strict interpretation of "actual knowledge" in s.164 (4) (a) of the Corporation Law would have resulted in the bank being able to assert the protective assumptions in s.164 (3). This is because despite the existence of suspicious circumstances, the bank did not actually know that the company seal had been affixed by a person unauthorised to do so.

To give protection to an outsider in these circumstances may encourage the outsider to refrain from making reasonable inquiries in the fear that such inquiries may lead to the acquisition of knowledge which would result in the loss of the protective assumptions. This would encourage outsiders such as lenders to don blinkers and perhaps unwittingly assist company officers to breach their duties or act without authority to the detriment of the company and its innocent shareholders or creditors. Mason CJ in the *Northside case* commented that to put a lender on inquiry in the circumstances of the case was to strike a fair balance between promoting business convenience and discouraging fraud and dishonesty. It would compel lending institutions to act prudently and thereby enhance the integrity of commercial transactions and morality.[50]

---

[50] (1990) 8 ACLC 611 at p 622

Perhaps in recognition of these policy considerations, the Full Court of the Supreme Court of Victoria in the *Brick and Pipe case* retracted form a strict interpretation of "actual knowledge" when it added:

> "What amounts to 'actual knowledge' is largely dependent on the facts and circumstances in a particular case and the inference they allow".[51]

The court was prepared to impute to the lender, the actual knowledge of its solicitor. It was not necessary to establish the actual knowledge of the lender itself. This means that the knowledge of an agent may be imputed as "actual knowledge" of a principal.

It is inconsistent to state that the term must be given its apparent meaning without elaboration and then to suggest that inferences may be drawn from what seems to be a deficiency in the drafting of s.164 (4) (a) of the Corporation Law. The Explanatory Memorandum to the 1983 Amendments indicated that s.164 was aimed at protecting outsiders who acted "in good faith" or were "innocent". In this regard the statutory provisions were intended to adopt the policy behind the common law Rule in *Turquand's case* and its exceptions. Gummow J in *Australian Capital Television Pty Ltd v Minister for Transport andCommunications*[52] thought that s.164 of the Corporation Law was not so much a "comprehensive code" as a provision designed to repair the failings of the common law.

---

[51] (1992) 10 ACLC 253 at p 264
[52] (1989) 7 ACLC 525 at p 535

It is difficult to argue that the inquiry exception to the Rule in *Turquand's* case is such a failure. The High Court in the *Northside case* strongly indicated that the common law inquiry exception was crucial in achieving the purpose of the Rule.

The strict wording of s.164 (4) (a) of the Corporation Law, which revolves around the term "actual knowledge", does not adequately incorporate the policy behind the common law principles. This has resulted in the courts showing some willingness to adopt a liberal interpretation of this term in order to arrive at a result which accords with the common law. This may mean the possible retention of the inquiry exception to the Rule in *Turquand's case* or something similar to it, despite its apparent removal in s.164 (4) (a) of the Corporation Law.

In considering whether an outsider should have the protection contained in the s.164 (3) assumptions, it seems that the good faith and probity of the outsider must be relevant so as to allow a consideration of their factors. This could be achieved by extending the operation of s.164 (4) (a) of the Corporation Law to include a situation where the outsider ought to know that a protective assumption is not correct. The limitation would then be attracted where the outsider is put on inquiry but fails to do so in circumstances such as arose in the *Northside case.* The implementation of this proposal would clarify the operation of the s.164 (4) (a) limitation in accordance with the policy of the section an obviate the need for judicial ingenuity by giving a strained interpretation to the words "actual knowledge". It is presently uncertain as to when inferences arise which would enable a court to deem an outsider as possessing actual knowledge when this cannot be

strictly shown.[53]

This extension of the limitation in s.164 (4) (a) of the Corporation Law to incorporate the inquiry exception would be consistent with equitable principles in relation to constructive trusts. A company may recover compensation from a third party who has assisted the company's officers in a dishonest transaction with knowledge of their breach of duty.[54] The meaning of "knowledge" in these constructive trust cases has been broadly interpreted so as to include knowledge that would have been gained by a reasonable person put on inquiry due to the circumstances. The law of constructive trusts applies to directors who act in breach of duty as well as trustees. Therefore under equitable principles, a company may seek a remedy for the recovery of property from a third party who made a "calculated abstention from inquiry."[55]

If the equitable rule gives a company greater scope to bring an action against an outsider to seek remedies to avoid the contract or recover property, a plaintiff company would be well-advised to rely, if possible, on the equitable rules which give a broad meaning to "knowledge". However this would require the company to firstly establish a breach of fiduciary duty by an officer. Section 164 of the Corporation Law does not require this.

The extent to which "actual knowledge" may be inferred also causes significant

---

[53] Lipton P "Holding out that a person is an Officer of the Company." (1991) 9 C&SLJ 404.

[54] *Consul Developments Pty Ltd v DPC Estates Pty Ltd* (1975) 132 CLR 373; *Baden Devaux and Lecuit v Societe Generale* [1983] BCLC 325; *Ninety Five Pty Ltd v Banque National de Paris* [1988] WAR 132.

[55] Lipton P "The Rule in Turquand's case : Past or Present ?" (1991)9 C&SLJ 37

uncertainty. For example it is difficult to determine whether actual knowledge exists in circumstances where the outsider is aware of various facts but may not have understood that these have a combined significance which if understood would have resulted in the acquisition of further actual knowledge. The circumstances where knowledge will be deemed under equitable principles of constructive trusts are quite clearly defined. These principles have evolved over a long period and it is difficult to determine the extent to which they may be incorporated into s.164 (4) (a) of the Corporation Law.

5.3.2. Where there is A Connection or Relationship with the Company

Section 164 (4) (b) of the Corporation Law provides for a second limitation which prevents a person dealing with a company from being entitled to make as assumption under s.164 (3). These assumptions cannot be made where the person's connection or relationship with the company is such that the person ought to know that the assumption is not correct.

This limitation appears to adopt something similar to the common law inquiry exception to the Rule in *Turquand's case* in situations where the person dealing with the company has a "connection or relationship" with the company. This limb of s.164 (4) of the Corporation Law may strengthen the argument that the first limb should be given a narrow reading in the interpretation of "actual knowledge".

The purpose behind the second limb of s.164 (4) of the Corporation Law appears to be the adoption of the common law principle that directors and other "insiders" of a

company generally cannot gain the protection of the Rule in *Turquand's case*.[56] This exception was restricted so as not to operate against a director who did not act as such in the particular transaction.[57] Section 164 (4) (b) of the Corporation Law does not refer to this distinction. Its terms are satisfied if there is a connection or relationship with the company, irrespective of whether the person acted for the company in the particular transaction.

The meaning of "connection or relationship" is therefore important to determine because only where this exists does the Corporation Law incorporate something similar to the common law inquiry exception to indoor management rule.

On this interpretation it would appear that s.164 (4) (b) of the Corporation Law has a narrow application so that it only applies to a non-arm's length connection or relationship where the person dealing with the company is an "insider". The Explanatory Memorandum states the purpose of the provisions as being to protect persons who are "innocent" and act in good faith. The existence of a connection or relationship which results in a non-arm's length dealing would strike at the innocence and good faith of the person dealing with the company.

This narrow interpretation of "connection or relationship" was adopted in *Lyford v Media*

---

[56] *Morris v Kanssen* [1946] AC 549.

[57] *Hely-Hutchinson v Brayhead* [1968] 1 QB 549.

Portfolio Ltd.[58] Media borrowed money from Broadlands and secured the loan by conferring a charge which was executed under the common seal of Media. The common seal was affixed and signed by a director who acted without authority. The articles of Media provided that the common seal could only be affixed with the authority of a resolution of the board. Such a resolution was not passed. Broadlands sought to enforce the charge and relied on the assumption of due sealing under s.164 (3) (e). Media argued that Broadlands was prevented form relying on this assumption because Broadlands and one of its directors had a relationship with the director of Media such that Broadlands ought to have known that the director of Media was acting without authority. This argument asserted that s.164 (4) (b) operated so as to prevent Broadlands form making the s.164 (3) (e) assumption. Nicholson J rejected this argument and gave s.164 (4) (b) of the Law a narrow operation. He held that it that it referred to knowledge that a person ought to have by reason of a connection or relationship with the company and not to knowledge which the person ought to have because of the circumstances of the transaction itself.

Obviously, a person who is a director, principal executive officer or secretary would have a connection or relationship with the company such that the person would be deemed to have knowledge of irregularities in the company's internal affairs. To allow an officer of the company the protection of the statutory indoor management rule would be "to encourage ignorance and condone dereliction of duty."[59] Such encouragement may arise

---

[58] (1989) 7 ACLC 271

[59] *Morris v Kanssen* [1946] AC at p 476.

where a director gained protection so as to enforce a transaction which was not beneficial to the company and also where directors are unaware of the articles of their company and whether the internal proceedings are properly carried out.

A non-arm's length relationship may also occur where the person dealing with the company is an employee or solicitor of the company or perhaps a major shareholder. A person may also be regarded as having a connection or relationship with the company for the purposes of the narrow view of s.164 (4) (b) of the Corporation Law where that person in involved in the operation of a group of companies of which the company with which he or she is dealing is a member.[60]

According to *Lyford v Media Portfolio Ltd*,[61] in order for the limitation contained in s.164 (4)(b) of the Corporation Law to apply, it is necessary to refer to all the circumstances which show the nature of the connection or relationship. It may then be assessed whether that connection or relationship was such that the person ought to have known that the assumption was incorrect.

Nicholson J did not extend "connection or relationship" to include an arm's length business relationship with past dealings. On the contrary, he considered that the past dealings indicated that the director of the chargor had the authority of the company to affix the common seal. This was because the lender knew the director was in day-to-day

---

[60] *Bell Resources Holdings Pty Ltd v Commissioner for ACT Revenue Collections* (1990) 93 ALR 354 at p 365.

[61] Ibid

control of the management and finances of the company, the company's office was the director's office and earlier borrowings in the name of the company had been concluded by the director.

The view of Nicholson J that the statutory provisions did not include the common law inquiry exception was supported by Studdert J in *Advance Bank Australia Ltd v Fleetwood Star Pty Ltd*[62] and the Full Court of the Supreme Court of Victoria in *Brick and Pipe Industries Ltd v Occidental Life Nominees Pty Ltd.*[63]

The narrow interpretation outlined above has the effect of giving an outsider greater scope under the statutory rules of enforce a contract despite refusing to make inquiries about an apparent irregularity, than was the position previously at common law. This is because the inquiry exception as applied in the *Northside case* only operates where the person dealing with the company has a legal or non-arm's length connection or relationship with company.

Recent cases in Australia have indicated a greater willingness by the courts to give the s.164 (4) (b) limitation a broader operation. A wider interpretation of "connection or relationship" was first suggested by the New South Wales Court of Appeal in *Storey v Advance Bank Aust. Ltd.*[64] Gleeson CJ indicated that it could arise out of "the very dealing which is putatively affected by the irregularity".

---

[62] (1992) 10 ACL703 at p 712. This case went on appeal as *Storey v Advance Bank Aust. Ltd* (1993) 11 ACL 624.

[63] (1992) 10 ACL 253 at p 262.

[64] (1993) 11 ACLC 624 at p 639.

The ambit of s.164 (4) (b) of the Corporation Law was considerably expanded in *Bank of New Zealand v Fiberi Pty Ltd.*[65] Priestley JA held that the connection or relationship between the bank and the company was such that the bank ought to have known that the persons who executed the guarantees did not have authority and therefore the bank could not rely on the protective assumptions.

Priestley JA focused on the meaning of the words "ought to know". He considered that these words required a judge,

> "to look at the person in question, consider the full factual circumstances of that person's connection or relationship with the company in regard to the particular matter in question and then decide whether in those circumstances that person acting reasonably would know the true position about the matter assumed."[66]

It would appear that an important consideration is if the outsider is a bank or other financial institution. In such cases, the outsider should have knowledge of the capital and shareholder structures of the company and the nature of lending transactions encourages prudent assessment of the circumstances. This is particularly the case where there is something unusual about those circumstances.

This formulation is similar to the common law inquiry exception even though Priestley JA considered that the concepts were different. The inquiry exception refers to the

---

[65] (1994) ACLC 48.

[66] (1994) 12 ACLC 48 at p 59.

existence of circumstances which require further inquiry. The "ought to know" concept requires consideration of what a person acting reasonable would have known in the circumstances.

On the facts of the *Fiberi case*, Priestley JA concluded that a reasonably competent and prudent bank official in the factual matrix in which the Bank's official was placed, would have seen to it that further information about the company officer's authority would have been obtained. "The obtaining of the information should have been a matter of no difficulty. Should there have been any difficulty, then the need for obtaining the information would become only more obvious.[67] Kirby P in the *Fiberi case* adopted a different approach to the interpretation of s.164 (4) (b) of the Corporation Law but came to the same conclusion as the majority judges. He also rejected the restrictive approach adopted in *Lyford's case* and stated that the connection or relationship did not have to be a "legal" one, nor did it refer only to a pre-existing or ongoing relationship.

Kirby P applied the underlying principles of the Rule in *Turquand's case* as expressed by the High Court in the *Northside case* and on the facts considered that the circumstances of the *Fiberi case* were stronger than those present in the *Northside case* so as to put the lender on inquiry. The facts which activated the requirement of inquiry included the following:

a) The transactions were for purpose apparently unrelated to the company's business and

---

[67] (1994) 12 ACLC 48 at p 59.

no apparent benefit was gained by it.

b) The outsider dealt with an ordinary director who purported to act for the company. The need for inquiry is stronger than would be the case if the dealings were with a managing director.

c) The property of the company which was dealt with was a residence and not acquired for commercial use. The property was used for the commercial purposes of other companies.

d) One of the persons who purported to act as an officer had not been named in the company returns lodged with the Commission.

It would seem that the approaches of both Priestley JA and Kirby P caused a sensible result to be reached in the *Fiberi case* which was accordance with the purpose of the legislation. However this has required a departure from a plain reading of the legislation. In particular, they do not address why s.164 (4) (a) of the Corporation Law precludes a person from making the protective assumptions only if that person has actual knowledge that an assumption is incorrect. The outsider is expressly required to make inquiry only where a connection or relationship with the company exists. According to the reasoning of the Court in the *Fiberi case*, a connection or relationship will generally arise where the circumstances of a transaction ought to lead to inquiries. In a circular way, this then triggers the "ought to know" exception in s.164 (4) (b) the Corporation Law.

The *Fiberi case* would appear to largely incorporate the inquiry exception to the indoor

management rule into the legislation by giving a wide reading to s.164 (4) (b) of the Corporation Law. On the other hand, the "actual knowledge" exception in s.164 (4) (a) of the Corporation Law would be correspondingly restricted because in many cases there will be a connection or relationship so that the inquiry exception will apply. It is the overall conduct of the outsider which should be considered, not primarily whether the outsider has a connection or relationship with the company in a narrow sense.

A person dealing with a company should lose the entitlement to rely on the protective assumptions where the person knows or ought to know that the assumption is incorrect. Any connection or relationship between the person and the company would be a relevant fact in determining what the person ought to know rather than the primary requirement which must be shown before the inquiry exception is activated. The crucial consideration is whether the outsider has acted innocently or bona fide so as to warrant reliance on the statutory assumptions.

5.4. Forgery

Section 166 of the Corporation Law provides that the s.164 (3) assumptions may be made in relation to dealings with a company even if a person referred to in s.164 (3) (b), (c) or (e) or an officer, agent or employee referred to in (d) or (f) acts fraudulently in relation to the dealings or has forged a document that appears to have been sealed on behalf of the company. The outsider loses this entitlement to make the assumptions where that person has actual knowledge that the officer, agent or employee of the company or the person held out as such acted fraudulently or forged a document.

The purpose of s.166 of the Corporation Law was stated in the Explanatory Memorandum as being to restate the common law rule in the *Northside case*[68] that a company will not escape liability for the acts of its officers, agents or employees merely because they have acted fraudulently, if the company would otherwise have been made liable by the fraudulent act. It also over-rules the interpretation placed on *Ruben v Great Fingall Consolidated*[69] that a forgery is a nullity and therefore comprises an exception to the Rule in *Turquand's case*.

Section 166 of the Corporation Law does not explain whether a fraudulent act for a forged document includes an unauthorised affixing of the company seal of whether it is restricted to the affixing of a seal or signatures which are not genuine. It probably refers only to a fake seal or signatures because unauthorised affixation of a genuine seal would be covered by s.164 (3) (a) and (e) in any case. Kirby P in the *Fiberi case* concluded that there was an overlap between s.164 (3) (a) and (e) and that paragraph (a) could be applicable to cases involving the use of the company seal.

He suggested that paragraph (a) did not operate where "the sealing" was carried out with a fake seal. This restriction on the operation of s.164 (3) (a) was evident because the references to the seal.[70] Where a seal which was not genuine was used, the outsider was still protected by s.164 (3) (e) of the Corporation Law. This is made clear by virtue of

---

[68] (1990) 8 ACLC 611 at p 617 per Mason CJ.

[69] [1906] AC 439.

[70] (1994) 12 ACLC 48 at p 58.

s.166 of the Corporation Law.

Kirby P found support for this approach in the Explanatory Memorandum accompanying the 1983 Amendments which stated that,

> "the purpose of the assumption in s.164 (3) (e) is to make it clear that a company will not be able to escape liability for fraudulently sealed documents."

This broad interpretation of s.164 (3) (e) would have enabled the lender in Fiberi to rely on this assumption despite the existence of forgery, but for the operation of the limitations contained in s.164 (4) of the Corporation Law.

Mason CJ in the *Northside case* expressed doubt that forgery was a true exception to the *Rule in Turquand's* case but thought that in any case it had a limited operation.[71] Section 166 of the Corporation Law clearly provides that forgery and fraud do not take away the entitlement of an outsider to rely on the protective assumptions unless the outsider has actual knowledge of the forgery or fraud.

---

[71] (1990) 8 ACLC 611 at p 617.

5.5 Conclusion

Therefore it may be concluded that though s.164(3) of the Corporation Law sought to codify and clarify the rule in Turquand's case, it is not a "comprehensive code" but a provision designed to repair the failings of the common law.

It has also to be highlighted that s.164(3) of the Corporation Law does not override the principles and policies of the common law unless this has been expressly stipulated by the legislation.

Further, it was not a universal and unconditional objective of the legislation to protect persons dealing with a company at the expense of all other competing considerations. The purpose is to protect persons who deal in good faith and innocently.

Chapter 6

CONCLUSION

A company operates through its two vital and constituent parts or organs: the board of directors and the general meeting of members. Wide powers of management are conferred on the board of directors. This is typical of most companies. Accordingly, when the board exercises those powers, its acts are regarded as the acts of the company. In other instances, the acts of the members in general meeting are considered as the acts of the company. Sometimes the board of directors delegate some of their powers to particular individuals, such as the managing director or the principal executive officer. The acts or state of mind of these individuals may be attributed to the company.

In practice, outsiders rarely deal with the board of directors or the members in general meeting. More often, its relationship with the company involves dealing with its agents or employees. Companies are capable of being bound by the acts of its agents in the same way as natural persons: s.35(4) of the Act. This involves the application of the principles of agency law, in particular the question whether those who purport to act on the company's behalf have the authority to do so. It can be seen that agency law has several distinct features in its application to companies.

The ultra vires doctrine was once a serious obstacle for those contracting with a company. As was indicated in this dissertation, ingenous drafting of the objects clause by clever draftsmen and legislative intervention by progress minded legislatures have reduced the effectiveness of the once dreaded ultra vires trap.

England, the original source of the Company Law of the Commonwealth has gone to almost the extent of granting full capacity to companies albeit with much caution and many safeguards. Australia has taken a bolder step and has given full legal capacity to companies. Both the English and Australian legislatures have recognised that some parts of the old doctrine are beneficial and must remain and therefore have preserved it in statutory provisions. In both countries the doctrine may sometimes (but rarely) rise from its grave and threaten both the outsider and the company.

In England, directors are under a duty to the company and its members to adhere to a company's objects clause. Again in England, a member could restrain a proposed ultra vires transaction provided that no legal obligation has arisen between the company and a third party. Australia has provisions in its Corporations Law which achieve similar results where the company chooses to state its objects clause in its memorandum of association. Both legislatures have abolished its constructive notice doctrine.

Malaysia has continued to pin its faith in its s.20 (1) of the Companies Act 1965. Section 20(1) abolishes the application of the doctrine between a company and a third party. An unusual feature of the Malaysian provision a member or a holder of a debenture secured by a floating charge can restrain performance of an ultra vires act even though a binding agreement has arisen between the company and a third party, as long as the transaction remains executory and remains to be performed. The power of members and debenture holders under a floating charge to restrain a legally binding agreement is a peculiarity of the Malaysian Companies Act. Although the third party may receive compensation by virtue of s.20(3), the compensation is limited. A pertinent question is whether Malaysia should adopt the English and Australian reforms.

An important point to note about the Malaysian statutory provisions on ultra vires is the absence of a clear and express provision abolishing the Common law doctrine of constructive notice. Thus technically it is possible for the courts to nullify the effect of s.20 (1) by ruling that the Common law doctrine still applies in Malaysia. The application of the Common law doctrine will make s.20 (1) a dead letter. Such a ruling is extremely remote bearing in mind the legislative intent behind s.20 (1). However, a clear statutory provision clarifying the position would be useful. In this context, the Australian statutory reform may be a useful provision to adopt. Again, where ultra vires can rear its offensive head, it must continually be borne in mind that its deals with the capacity of the company and is not ratifiable by using the agency principles.

Even where s.20 of the Act prevents a company from defeating a transaction by pleading ultra vires it can do so by asserting a breach of authority of its agents and which breach was known to the other party to the transaction.

With regards the actual authority of an agent, it is a relationship between the principal and the agent; the rest of the world is a stranger to this relationship. The third party dealing with the agent of a company does not know what the agent's actual authority is, nor in most cases can he find out. Sometimes the authority of agent to do certain acts depends on compliance with certain formalities or there is some irregularity in the management which vitiates the authority conferred upon the agent. A party outside the company has no way of determining whether the company's internal regulations have been complied with.

However, the law does not require an outside party to do so. If an agent has an apparent authority to do an act, a person dealing with the company is entitled to assume that all

matters of internal management and procedure prescribed by the articles of association have been complied with. This is known as the "rule in *Turquand's* case" or the "indoor management rule" .

History has shown that, despite its noble intention to protect outsiders dealing with a company, the Rule became increasingly obscure and uncertain with the passing years. The Rule was subject to irreconcilable decisions and unacceptable distinctions for modern company law

As a consequence, in Australia, the common law principles discussed above have been now been replaced by statutory provisions, in particular s.164(3) of the Corporation Law.

It has also to be highlighted that s.164(3) of the Corporation Law does not override the principles and policies of the common law unless this has been expressly stipulated by the legislation.

Further, it was not a universal and unconditional objective of the legislation to protect persons dealing with a company at the expense of all other competing considerations. The purpose is to protect persons who deal in good faith and innocently.

One conclusion seems to be inevitable. Although s.164(3) of the Corporation Law sought to codify and clarify the rule in Turquand's case, it is not a "comprehensive code" but a provision designed to repair the failings of the common law.

Early indications are that the section will be subject to minute scrutiny by the judiciary and be subject to numerous decisions. One fear may be that whether the imposition of the interpretation upon interpretation may lead to the uncertainties which the exception to the *Turquand's* rule itself are subject to. The judicial development of s.164(3) of the Corporation Law will be an interesting topic for the future.

In Malaysia the Rule in *Turquand's* case reigns supreme together with its obscurities and inadequacies. Whether the Malaysian legislatures may be prompted or be tempted to venture into a statutory reform like in Australia or as in England remains to be seen. For the time being in Malaysia the subject of this dissertation continues to be regulated by common law, which to an Australian or English observer, may look a little out of date. Finally, it may be stated that while reform is welcome and necessary, a bland automatic adoption of foreign legislation may not be to Malaysia's advantage. Care must be taken to ensure that we do not import foreign legislation with all their deficiencies.

BIBLIOGRAPHY

Arjunan K and Low C K Lipton and Hertberg's Understanding Company Law in Malaysia 1st ed 1995 LBC Information Services

Austin RP "Constructive Trusts" in Finn P D Essays in Equity (1985) Law Book Co..

Balan and Talat Mahmood " Doktrin Ultra Vires dan Seksyen 20 Akta Syarikat 1965"- an article about to be published in the Journal of Malaysian & Comparative Law"

Calvert, H "Constructive Notice and Illiteracy in Singapore and Malaya" [1959] MLJ lxv.

Campbell I D "Contracts with Companies " (1959) 75 LQR 469.

Carroll R " Proper Performance of Duties by Company Officers: the Statutory Assumption in s.164(3) (f) of the Corporation Law" (1995) 69 ALJ 200.

Explanatory Memorandum to the Companies and Securities Legislation (Miscellaneous Amendments) Act 1983.

Farrar Farrar's Company Law 3rd ed 1991 Butterworths.

Ford H A J and Austin R P Principles of Corporations Law 7th ed Butterworths 1995.

Gower L C B Modern Company Law 2nd ed 1957 Stevens.

Gower L C B Modern Company Law 5th ed 1992 Sweet and Maxwell.

Guide to Company Law In Malaysia and Singapore 1995 CCH Asia Limited

Halsbury's Laws of England 4th ed 1988 Vol. 7 (1).

Harpum C "The Stranger as Constructive Trustee" (1986) 102 LQR 114 and 267.

Heydon J D " Recent Development in Constructive Trusts" (1977) 51 ALJ 635.

Leow C S " The Applicability of the Turquand Rule to Corporate Acts: Northside Developments Property Ltd. v. Registrar General" (1991) 3 MLJ.

Lipton & Hertzberg Understanding Company Law 5th ed (1995)

Lipton P "Holding Out that a Person is an Officer of the Company" (1991) 9 C& SLJ 37.

Lipton P " The Inquiry Exception to the Rule in Turquand"s Case: Past or Present?" . (1991) 9 C&SLJ.

Low S C Corporate Powers – Controls, Remedies and Decision-making 1st ed (1996) Malayan Law Journal Sdn. Bhd.

Mayson, French & Ryan Company Law 1991 Blackstone

Montrose J L "Apparent Authority of an Agent of a Company" (1934) 50 LQR 224.

Ong D S K " The Rule In Turquand's Case: Estoppel Without Representation" (1992) 66 LIJ 70

Ong – Wee P "Ultra Vires and Agency – Untwined and Entwined? Public Bank Bhd. v. Metro Construction Sdn. Bhd. [1992] 2 MLJ cv.

Pennington Company Law 6th ed (1990) Butterworths

Sealy Cases and Materials in Company Law 1996 Butterworths

Sievers A.S. " Farewell to the Sleeping Director – The Modern Judicial and Legislative Approach to Directors' Duties of Care, Skill and Diligence – Further Developments ." (1993) 21 ABLR 111.

Thompson A R "Company Law Doctrines and Authority to Contract " (1956) 11 Univ. of Toronto LJ 248

Walter Woon Company Law 7th ed (1997) Longmans.